(17)

No. 88-2109-CFX   Title: Kansas and Missouri, etc. Petitioners
Status: GRANTED   v.
                          Utilicorp United Inc.

Docketed: Court: United States Court of Appeals
June 26, 1989   for the Tenth Circuit

Counsel for petitioner: Ward,R. Lawrence

Counsel for respondent: Bartlit Jr.,Fred H., Klein,Joel I., Sanders Sr.,William H.

Entry	Date	Note	Proceedings and Orders
1	Jun 26 1989	G	Petition for writ of certiorari filed.
2	Jul 24 1989		Brief amici curiae of Alaska, et al. filed.
3	Jul 25 1989		Brief of respondents Kansas Power & Light Co., et al. in opposition filed.
4	Aug 2 1989		DISTRIBUTED. September 25, 1989
5	Aug 18 1989	X	Reply brief of petitioner Kansas filed.
6	Sep 1 1989	X	Supplemental brief of petitioner Kansas filed.
7	Oct 2 1989	P	The Solicitor General is invited to file a brief in this case expressing the views of the United States.
8	Dec 20 1989		REDISTRIBUTED. January 12, 1990
9	Dec 20 1989	X	Brief amicus curiae of United States filed.
10	Jan 16 1990		Petition GRANTED.
			**
11	Feb 13 1990		Record filed.
		*	Certified copy of original record and C. A. Proceedings,box, received.
12	Feb 23 1990		SET FOR ARGUMENT MONDAY, APRIL 16, 1990. (2ND CASE)
13	Feb 28 1990		Joint appendix filed.
14	Feb 28 1990		Brief of petitioner Kansas filed.
15	Mar 2 1990		Brief amici curiae of Forty Six States filed.
16	Mar 2 1990		Brief amici curiae of National Conference of State Legislatures, et al. filed.
17	Mar 2 1990		Brief amicus curiae of Illinois filed.
18	Mar 2 1990	G	Motion of Nancy Allevato, Personal Representative of Michael J. Ferrantino, Sr., Deceased, for leave to file a brief as amicus curiae filed.
25	Mar 2 1990		Brief amicus curiae of United States filed.
20	Mar 15 1990	G	Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument filed.
19	Mar 19 1990		Motion of Nancy Allevato, Personal Representative of Michael J. Ferrantino, Sr., Deceased, for leave to file a brief as amicus curiae GRANTED.
21	Mar 22 1990		The writ of certiorari as to respondent Kansas Power & Light Co. dismissed pursuant to Rule 46.
23	Mar 23 1990		CIRCULATED.
22	Mar 26 1990		Motion of the Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument GRANTED.
24	Mar 30 1990	X	Brief amicus curiae of Washington Legal Foundation filed.
26	Apr 2 1990	X	Brief amicus curiae of United States filed.

No. 88-2109-CFX

Entry	Date	Note	Proceedings and Orders
27	Apr 2 1990	X	Brief of respondent Utilicorp United Inc. filed.
28	Apr 6 1990	X	Reply brief of petitioners Kansas and Missouri filed.
29	Apr 16 1990		ARGUED.

88-2109

No.

In the Supreme Court of the United States

OCTOBER TERM, 1988

THE STATES OF KANSAS AND MISSOURI,
AS *PARENS PATRIAE*,
Petitioners,

vs.

THE KANSAS POWER & LIGHT COMPANY

and

UTILICORP UNITED, INC.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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QUESTIONS PRESENTED

1. Do residential indirect purchasers of natural gas, represented *parens patriae* by their state attorneys general, have standing to sue under Section 4 of the Clayton Act, where there is an easily-proven, 100% pass-on of illegal overcharges, effected by federal and state regulations rather than by a fixed-quantity cost-plus contract?

2. Where federal and state regulations require that the full amount of any illegal overcharge be passed on by the direct purchaser in readily-identifiable form, is there an exception to the general rule barring indirect purchaser antitrust suits under Section 4 of the Clayton Act?

PARTIES

Petitioners, the States of Missouri and Kansas, acting as *parens patriae* on behalf of their residential gas consumers, are two of the six plaintiffs in a consolidated proceeding known as *In re Wyoming Tight Sands Antitrust Cases*. The States were appellants in the Tenth Circuit proceeding from which this petition arises.

Appellees in the Tenth Circuit included plaintiff The Kansas Power & Light Company ("KPL"), intervenor UtiliCorp United, Inc. ("UtiliCorp," which includes its two subsidiaries, Missouri Public Service Company and Kansas Public Service Company), and plaintiff Kansas Gas & Electric Company ("KG&E"). Plaintiff Farmland Industries, Inc. did not take part in the Tenth Circuit appeal. Because the issues raised in this Petition do not affect KG&E[1] or Farmland, only KPL and UtiliCorp are named as respondents herein.

Defendants below were Amoco Production Company ("Amoco"), Cities Service Oil & Gas Corporation ("Cities Service"), CSG Exploration Company ("CSGE"), Williams Natural Gas Company ("Pipeline") and two limited partnerships, Moxa Limited Partnership and Wamsutter Limited Partnership. Amoco, Cities Service and CSGE intervened at the Tenth Circuit, but did not take a position as to which group of plaintiffs should prevail. The other defendants did not appear in the Tenth Circuit. None of the defendants is named as a respondent herein.

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1. Plaintiff Kansas Gas & Electric is solely an electric utility that does not resell gas. The States did not oppose KG&E's motion for partial summary judgment, and have recognized throughout these proceedings that summary judgment was properly granted in favor of KG&E.

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No.

In the Supreme Court of the United States

OCTOBER TERM, 1988

THE STATES OF KANSAS AND MISSOURI,
AS *PARENS PATRIAE*,
Petitioners,
vs.
THE KANSAS POWER & LIGHT COMPANY
and
UTILICORP UNITED, INC.,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

The States of Missouri and Kansas, appearing here in their *parens patriae* capacity on behalf of all natural persons in these States who are residential natural gas consumers, respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Tenth Circuit entered in this proceeding on January 31, 1989, in order to resolve the conflict between the Tenth and Seventh Circuit Courts of Appeals on the important issues presented herein.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Tenth Circuit that gives rise to this petition is reported at *In re Wyoming Tight Sands Antitrust Cases,* 866 F.2d 1286 (10th Cir. 1989), and is reprinted in Appendix A hereto ("App. A") at page A1. By order filed March 27, 1989, the Tenth Circuit denied the petition for rehearing and suggestions for rehearing en banc. App. B, A18.

The opinion of the United States District Court for the District of Kansas dismissing petitioners' *parens patriae* complaints is reported at *In re Wyoming Tight Sands Antitrust Cases,* 695 F. Supp. 1109 (D. Kan. 1988), App. C, A22; the district court's opinion on the motion for certification is reported at 695 F. Supp. at 1119, App. D, A40.

JURISDICTION

On May 4, 1988, the district court granted partial summary judgment in favor of the respondent utilities and dismissed the federal antitrust claims of the States of Kansas and Missouri as *parens patriae* "for lack of standing." On motion of the States, the district court on June 7, 1988, certified to the Tenth Circuit a question of *parens patriae* standing, pursuant to 28 U.S.C. § 1292(b). The Tenth Circuit accepted the Section 1292(b) appeal.

On January 31, 1989, the Tenth Circuit entered an opinion affirming the decision of the district court. A timely-filed petition for rehearing and suggestion for rehearing en banc was denied on March 27, 1989. Pursuant to 28 U.S.C. § 2101(c), this petition for certiorari has been filed within 90 days of the denial of rehearing.

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTE INVOLVED IN THE CASE

Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982), provides in pertinent part:

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

STATEMENT OF THE CASE

A. Background

In 1984, 1985 and 1986, the Attorneys General for the petitioners States of Kansas and Missouri (hereinafter "the States") and three utilities filed these actions charging defendant Williams Natural Gas Company ("Pipeline") and others with selling natural gas at artificially inflated prices. The inflated prices, plaintiffs allege, were the result of a price-fixing conspiracy and other anticompetitive behavior involving Pipeline, its then-parent Cities Service Company, CSG Exploration, Amoco and two limited partnerships. The general background of the conspiracy is described in *Midwest Gas Users Association v. FERC,* 833 F.2d 341 (D.C. Cir. 1987).

The price-fixed gas was produced in Wyoming, then transported by Pipeline and sold to KPL, UtiliCorp and

other utilities in Missouri and Kansas.[2] The utilities resold the gas to various consumers, including individual residents of the two States. These gas sales occurred under a regulatory system that required *all* gas costs to be passed on by the Pipeline, through the utilities, to the end-use consumers.[3] This regulatory pass-through mechanism is mandatory; at no level of distribution is there any discretion to absorb or modify any increase in the cost of gas.[4] The effect of this pass-through on the

2. KPL and UtiliCorp are two of more than 50 gas utilities operating as regulated monopolies within defined service areas in Kansas and Missouri. Other non-party utilities provide natural gas purchased from the conspirators to over 50,000 Kansas residential consumers. The claims of these residential users will be lost if the Attorneys General cannot represent them in their *parens patriae* capacity.

3. This regulatory mechanism operates first at the federal level, where the Pipeline is regulated by the Federal Energy Regulatory Commission (FERC), pursuant to the Natural Gas Act, 15 U.S.C. §§ 717 *et seq.* (1982) (NGA), and the Natural Gas Policy Act, 15 U.S.C. §§ 3301 *et seq.* (1982) (NGPA). Under the NGA, Pipeline must adjust its rates semi-annually to reflect any changes in the price of gas paid to producers by Pipeline, in accordance with Purchased Gas Adjustment (PGA) clauses in Pipeline's tariff. 15 U.S.C. § 717(d), (e); *see* 18 C.F.R. §§ 154.1 *et seq.* (1988).

At the state level, utilities such as KPL and UtiliCorp are regulated by the Missouri Public Service Commission and the Kansas Corporation Commission. *See* Mo. Rev. Stat. §§ 386.250 (5), 393.140(1), 393.270(2) (1986); Kan. Stat. Ann. §§ 66-1,201, 66-1,206 (1985). Both state commissions enforce PGA clauses in the utilities' tariffs. UtiliCorp's KPS subsidiary operates under a PGA clause in a locally-enforced ordinance. These PGAs require that KPL and UtiliCorp automatically pass on to their customers the utilities' entire wholesale cost of gas from the Pipeline.

4. As David S. Black, President and CEO of KPL, testified before the Kansas Legislature:

> Essentially, we [KPL] provide a transportation service, and have title to the gas for the few hours required to move it from the wellhead to the burner-tip. As the cost of this gas changes, it is reflected in the customers' bills, through the operation of the purchased gas adjustment mechanism, penny-for-penny and dollar-for-dollar.

cost of gas to consumers is easy to determine—the utilities make public filings showing the volume and price of gas sold to each customer category, including residential consumers; further, the passed-on prices are reflected as a separate identifiable entry on each residential consumer's monthly gas bill from the utilities.

The Tenth Circuit, recognizing the effect of this regulatory system, *assumed* for purposes of its decision "that there was a perfect and provable pass-on of the allegedly illegal overcharge . . ." App. A, A14.

B. Proceedings Below

The utilities, in motions for partial summary judgment, argued to the district court that they alone were the proper plaintiffs and that the States lacked standing to sue because residential consumers are indirect purchasers whose claims are barred by the rule of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968) and *Illinois Brick Company v. Illinois*, 431 U.S. 720 (1977). Although the utilities did not deny that they passed on all of the overcharges to the residential consumers, they argued that because they had no fixed-quantity contracts with these consumers, no exception to the direct-purchaser rule applied. Petitioners countered that because state and federal regulation resulted in an easily-provable and perfect pass-through of all illegal overcharges, they had standing to sue under the *Illinois Brick* exception. The district court granted summary judgment in favor of the utilities, holding that even proof of a perfect pass-on would not give the States standing, because there were no "fixed-quantity contracts." App. C, A33-34.

On interlocutory appeal, the Tenth Circuit affirmed the district court's dismissal of the States' *parens patriae*

claims. While recognizing that "there might be" an exception to the *Hanover Shoe* and *Illinois Brick* rule that only direct purchasers have standing to sue, the Tenth Circuit found no exception applicable here. Even though it assumed a perfect pass-through of damages to the consumer, the court narrowly interpreted *Illinois Brick* as *requiring* a pre-existing, fixed-quantity, cost-plus contract. The Court of Appeals held that because no "fixed-quantity contract" was present in this case, the consumers had no standing.[5]

In so holding, the Tenth Circuit squarely rejected the carefully-reasoned decision of the en banc Seventh Circuit on virtually identical facts in *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Corporation*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S. Ct. 543 (1988).[6] There, Judge Richard Posner expressly allowed residential consumers of natural gas to maintain *parens patriae* actions. The Seventh Circuit concluded that the regulatory system under which natural gas is produced, distributed and consumed operates to alleviate any concerns expressed in *Illinois Brick*. Specifically, the Seventh Circuit found that this regulation resulted in a perfect and easily-provable pass-through of antitrust damages to residential consumers which would (1) obviate any need to apportion these damages and (2) provide state attorneys general with incentive to sue.

5. In the Tenth Circuit's words: "To say that the utilities have a cost-plus fixed fee contract for a fixed quantity with their residential consumers would amount to fitting a square peg into a round hole. There exists no contract between the utilities and their residential consumers for any particular quantity." App. A, A12.

6. For the convenience of the Court, a copy of this decision is included in Appendix E hereto, at A43.

In rejecting the Seventh Circuit's approach, the Tenth Circuit mechanically applied certain language from *Illinois Brick* without analyzing the underlying concerns expressed by this Court. App. A, A8-13. The Tenth Circuit assumed "that there was a perfect and provable pass-on of the allegedly illegal overcharge . . . ." App. A, A14. Nevertheless, the court found that this was not a sufficient reason to allow indirect purchasers to sue for an antitrust violation:

> A perfect pass-on, standing alone, is not sufficient reason to allow an indirect purchaser to sue [sic] an alleged antitrust violation. We narrowly construe the cost-plus exception as to do otherwise would be to do that which the Supreme Court has cautioned against. We hold that the controlling cases are *Hanover Shoe* and *Illinois Brick*, and not *Panhandle Eastern*. App. A, A14-15.

The Tenth Circuit concluded that even *considering* proof of a perfect pass-on would "'entail the very problems that the *Hanover Shoe* rule was meant to avoid.' *Id.* at [431 U.S.] 744-45. We therefore hold that the amount of illegal overcharges actually passed on by the utilities to its customers is not an issue of material fact necessary to a resolution of the narrow issue before this court." App. A, A17.

The States' petition for panel rehearing and/or rehearing en banc was denied.

Thus the issue presented is purely a question of law on undisputed facts: where there exists a mandatory, readily-proven pass-through of overcharges, which holding is correct—that of the court below in this case, or that of the Seventh Circuit in *Panhandle Eastern*?

REASONS FOR GRANTING THE WRIT

The Tenth Circuit's decision in this case directly conflicts with the holding of the Seventh Circuit in *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Corporation*, 852 F.2d 891 (7th Cir.) (en banc) (Posner, J.), *cert. denied*, 109 S. Ct. 543 (1988), App. E, A43. There, the en banc Seventh Circuit fleshed out the "cost-plus" exception and applied it to permit the Illinois attorney general, acting as *parens patriae* on behalf of residential gas consumers, to sue for antitrust damages. Specifically, the critical question on which the Seventh and Tenth Circuits disagree is: Do indirect purchasers, who by regulatory mandate pay *all* of the illegal antitrust overcharges, fall within an exception to the general rule that only direct purchasers of a product have standing to seek antitrust damages from antitrust violators? The Seventh Circuit says "yes"; the Tenth Circuit says "no".

This conflict has resulted because lower courts are having significant problems understanding and interpreting prior opinions of this Court. These conflicting decisions complicate the uniform administration of Section 4 of the Clayton Act and undermine the ability of state attorneys general to enforce the antitrust laws. The Court should grant certiorari and end this confusion.

More specifically, the reasons for granting certiorari may be stated as follows:

I.

The Tenth Circuit's Decision Directly Conflicts With the Seventh Circuit's En Banc Ruling in Panhandle Eastern.

The conflict between the decision below and the Seventh Circuit's decision in *Panhandle Eastern*, App. E,

A43, is clear and complete. As the Tenth Circuit put it: "The States urge us to apply the law as enunciated in *Panhandle Eastern*, 852 F.2d 891. This we decline to do." App. A, A13.[7]

The Seventh Circuit in *Panhandle Eastern* found a complete and provable pass-through of allegedly illegal overcharges to residential consumers in Illinois. Based on this finding, the Seventh Circuit concluded that those consumers had standing to sue. The Tenth Circuit in the instant case *assumed* a 100% perfect pass-through of overcharges, yet nonetheless ruled that residential consumers were without standing, simply because they were indirect purchasers without a fixed-quantity contract.

These two cases are identical in every important factual respect. In both, state attorneys general sued to redress antitrust violations that resulted in injury to residential gas consumers. In both, the interplay between state and federal regulation required a perfect pass-on of the overcharges. In both, some or all of the utilities were also plaintiffs, despite the likelihood that any overcharges they collected might be ordered refunded to the consumers. In neither case were there problems with duplicative recovery or apportionment of shared damages, nor were there any real concerns for antitrust enforcement.

Under these circumstances, the Seventh Circuit held that the State could sue, reasoning that where the rationale for *Illinois Brick* does not apply, neither should

7. The district court also recognized the factual similarity between this case and *Panhandle Eastern*. It specifically relied on the Seventh Circuit's *panel* opinion in *Panhandle Eastern* (later reversed en banc) to support its entry of summary judgment: "Just recently the Seventh Circuit came to the same conclusion *on almost identical facts*" (emphasis added). App. B at A36.

the rule. The Tenth Circuit expressly disagreed. App. A, A13-15. The conflict is clear. Certiorari is thus appropriate.[8]

II.

The Decision Below Raises Important Issues as to the Standing of Consumers to Recover Antitrust Damages for Overcharges That Have Been Passed on to Them.

Three times this Court has suggested to lower courts that there is an exception to the general rule that only a direct purchaser has standing to recover antitrust damages: *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 494 (1968) ("there might be" an exception to the rule, "for instance, where an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged"); *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 735-36 (1977) ("*Hanover Shoe* indicated the narrow scope it intended for any exception . . . by citing, as the only example . . . a pre-existing cost-plus contract"); *California v. ARC America Corp.*, 109 S. Ct. 1661, 1666 n.6 (1989) (in *Illinois Brick* "we implicitly recognized . . . that indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them"). But the precise nature and scope

8. The *Panhandle Eastern* petition for certiorari presented two questions: (1) whether the Seventh Circuit's holding "in effect" overruled *Illinois Brick;* (2) whether "residential indirect purchasers of natural gas, who do not purchase gas pursuant to pre-existing, fixed quantity, cost-plus contracts with the direct purchaser," are barred from seeking antitrust damages by *Illinois Brick*. Those two questions mirror the ruling of the Tenth Circuit in the instant case, thus further underlining the conflict between the two Circuits.

of this exception has not been addressed or explained by this Court. The result is confusion and conflict in the lower courts.[9]

As noted in *California v. ARC America*, this Court in *Illinois Brick* was concerned "not merely that direct purchasers have sufficient incentive to bring suit under the antitrust laws . . . but rather that at least *some* party have sufficient incentive to bring suit." (Emphasis added). And the Court added in *ARC America* that "indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them," citing *Illinois Brick*. 109 S. Ct. at 1666 n.6. The facts in the present case fit precisely the situation described in the *ARC America* footnote, thereby suggesting that the Tenth Circuit's concerns are not shared by this Court. As indirect purchasers, the present consumers have "sufficient incentive" because they are represented by vigilant state attorneys general, well aware of their *parens patriae* responsibilities.

9. This is reflected in the decisions of several district courts applying the "cost-plus" exception in a regulatory environment. In *In re New Mexico Natural Gas Antitrust Litig.*, 1982-1 Trade Cas. (CCH) ¶ 64,685 (D.N.M. 1982), the court held, on facts similar to those here, that indirect purchasers could sue because public utility regulation had created "a straight cost pass through." *Id.* at 73,722. Other district courts have rejected an exception for cost-plus rate regulation. *See Go-Tane Service Stations, Inc. v. Ashland Oil, Inc.*, 508 F. Supp. 200 (N.D. Ill. 1981); *City of Cleveland v. Cleveland Elec. Illuminating Co.*, 538 F. Supp. 1306, 1323-24 (N.D. Ohio 1980); *U.S. Oil Co. v. Koch Refining Co.*, 518 F. Supp. 957, 962-63 (E.D. Wis. 1981). *See also In re Beef Indus. Antitrust Litig.*, 600 F.2d 1148 (5th Cir. 1979), *cert. denied*, 449 U.S. 905 (1980) (applying a test using the "functional equivalent" of a cost-plus contract).

And precisely because the gas utilities are highly regulated by the states and the overcharges are easily retrieved from public filings, this is also a case "in which it would be easy to prove the extent to which the overcharge was passed on to them [the residential gas consumers]."

If the Court is ever to explicitly recognize an exception to the direct-purchaser rule, this case presents the ideal opportunity. Each of this Court's underlying concerns in *Illinois Brick* is satisfied on the present record. Not only is the pass-on of overcharges complete and automatic, but it is easily shown by uncomplicated proof. Not only are the ultimate consumers the truly-injured parties, but here they have ample incentive to sue through their state attorneys general as *parens patriae*.

The Tenth Circuit ignored the underlying rationale of *Illinois Brick* and *Hanover Shoe*, choosing instead to rigidly apply the "fixed-quantity cost-plus contract" language of *Illinois Brick*. Is the Tenth Circuit correct? Must a pass-on arrangement always be accompanied by a cost-plus contractual obligation to purchase a fixed amount of the product? Or, as Judge Posner recognized, is it enough that the direct purchaser "acts like" a fixed-quantity reseller, with every incentive to pass on the entire overcharge? *See Panhandle Eastern*, App. E, A52-53. Would recognition of the standing of residential consumers to seek antitrust damages, in the context of a highly regulated industry, truly require—in the words of the Tenth Circuit—"carving out yet another exception (regulation of public utilities) to the basic rule that only a direct purchaser may sue for the antitrust violation"? App. A, A15.

This Court should grant certiorari to determine if residential gas consumers who are forced to absorb all the illegal overcharges, and who have sufficient incentive when represented by their state attorney general, have standing to seek treble antitrust damages. Does this situation constitute an exception to the basic rule that only direct purchasers have standing? Is this not precisely the situation contemplated in the *ARC America* footnote? None of these questions are answered by *Hanover Shoe, Illinois Brick*, or *ARC America*. But they are questions that repeatedly plague the lower courts, as shown by the conflict here. The Tenth Circuit decision squarely presents these questions. They are questions that deserve answers by this Court.

III.

The Issues in This Case Are Important to the Attorneys General of All Fifty States.

The Tenth Circuit's decision, barring the Attorneys General of Missouri and Kansas from suing to protect their residential gas consumers from antitrust violations, creates profound problems for attorneys general in all the States. The Kansas Attorney General, residing in the Tenth Circuit, cannot bring suit for his State's citizens. Nor can the attorneys general of other states, if suit is filed in the Tenth Circuit. But in the Seventh Circuit, these same suits by attorneys general may proceed without hindrance. Which decision should guide the actions of attorneys general in the other Circuits? The Sherman Act contemplates uniform interpretation and application across the United States. The conflict posed by the Seventh and Tenth Circuit decisions renders such uniformity impossible.

Congress placed state attorneys general in a preferred position in the enforcement of federal antitrust laws. The Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 15c (1982), "carves out a special place for state governments in enforcing federal antitrust laws." *In re Grand Jury Investigation of Cuisinarts, Inc.*, 665 F.2d 24, 35 (2d Cir. 1981). "In effect, the thrust of Title III of the Act was to overcome obstacles to private class actions through enabling state attorneys general to function more efficiently as consumer advocates." *Id.; see also* H.R. Rep. No. 499, 94th Cong., 2d Sess. 8 *reprinted in* 1976 U.S. Code Cong. & Admin. News 2578. The purpose of the Act—efficient enforcement of antitrust laws by the states—has been frustrated by the Tenth Circuit's substitution of private utilities as antitrust plaintiffs in lieu of state attorneys general.

The attorneys general have been left in a quandary as to the limits of their *parens patriae* authority in antitrust actions. While the Hart-Scott-Rodino Act and the *Panhandle Eastern* decision grant broad authority to state attorneys general, the decision below severely limits that authority and restricts the right of consumers to recover for injuries they have suffered. Thus both consumers and state attorneys general are vitally concerned that the Tenth Circuit's ruling be reviewed by this Court.

CONCLUSION

For the foregoing reasons, this petition for writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A

(Filed January 31, 1989)

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

Nos. 88-2158
88-2159

In re

WYOMING TIGHT SANDS ANTITRUST CASES.

STATE OF KANSAS, as parens patriae on behalf of natural person residing in Kansas, ROBERT T. STEPHAN, Attorney General of the State of Kansas,

and

STATE OF MISSOURI,
Plaintiffs-Appellants,

KANSAS POWER & LIGHT COMPANY, a Kansas Corporation; KANSAS GAS & ELECTRIC COMPANY,
Plaintiffs-Appellees,

UTILICORP UNITED INC.,
Plaintiff-interventor-Appellee.

v.

AMOCO PRODUCTION CO.; CITIES SERVICE OIL AND GAS CORPORATION, f/k/a Cities Service Company; CSG EXPLORATION COM-

PANY; WILLIAMS NATURAL GAS COMPANY, f/k/a Northwest Central Pipeline Corporation; THE WAMSUTTER LIMITED PARTNERSHIP; THE MOXA LIMITED PARTNERSHIP,
Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS
(D.C. Lead No. CIV. 85-2349-S)

Thomas J. Greenan of Ferguson & Burdell, Seattle, Washington (Robert T. Stephan, Attorney General for the State of Kansas; William L. Webster, Attorney General for the State of Missouri; Donald D. Barry and Deborah Farrar of Donald D. Barry, Chtd., Topeka, Kansas; James E. Hurt of Ferguson & Burdell, Seattle, Washington; Jack C. Chestnut of Chestnut & Brooks, P.C., Minneapolis, Minnesota; Thomas H. Brill, Kansas City, Missouri; R. Lawrence Ward, Jennifer Gille Bacon, Russell S. Jones, Jr., and Ann E. Carlson of Shughart, Thomson & Kilroy, P.C., Kansas City, Missouri, with him on the briefs), for Plaintiffs-Appellants State of Kansas and State of Missouri.

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Sally R. Burger (William H. Sanders, Sr., Floyd R. Finch, Jr., and Katharine Bunn of Blackwell Sanders Matheny

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Kirkland & Ellis, Chicago, Illinois; Watson, Ess, Marshall & Enggas, Olathe, Kansas, on the brief for Defendant-Appellee Amoco Production Co.

Skadden, Arps, Slate, Meagher & Flom, Washington, D.C.; Stinson, Mag & Fizzell, Kansas City, Missouri, on the brief for Defendants-Appellees Cities Service Oil and Gas Corporation and CSG Exploration Company.

Before SEYMOUR, MOORE, and BRORBY, Circuit Judges.

BRORBY, Circuit Judge.

This appeal involves a single issue: May residential consumers who are indirect purchasers of natural gas maintain an antitrust suit against the alleged antitrust violators?

I.

Three investor-owned public utilities, the Kansas Power & Light Company, Kansas Gas & Electric Company, and UtiliCorp United Inc., filed separate complaints against defendants Amoco Production Co., Cities Service Oil and Gas Corporation, CSG Exploration Company, The Moxa Limited Partnership, and The Wamsutter Limited Partnership, alleging, *inter alia*, that all defendants illegally conspired to artificially inflate the price of natural gas produced from various natural gas fields in Wyoming. The gas was then transported and sold to the public util-

ities by the conspiring defendant, Williams Natural Gas Company, an interstate pipeline company.

The states of Kansas and Missouri (the States) filed similar suits wherein basically they asserted two types of claims against the same defendants: (1) on behalf of residential consumers who purchased natural gas from the public utilities, the States acting in a *parens patriae* capacity; and (2) on behalf of state agencies, municipalities, and other political subdivisions that purchased gas directly from Williams Natural Gas Company. These suits were consolidated.

The defendants asserted various defenses, including allegations that the public utility plaintiffs lack standing under § 4 of the Clayton Act, 15 U.S.C. § 15 (1982), in that plaintiffs had not been injured in their business or property because the public utilities had passed on illegal increases in the price of natural gas to the ultimate consumer who paid the entire cost of antitrust injuries. The public utilities then filed motions for summary judgment to prohibit these pass-on defenses under *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968).

The trial court granted partial summary judgment in favor of the public utilities prohibiting the use by the defendants of the pass-on defense. The trial court characterized the motions as "in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity," and *sua sponte* dismissed the *parens patriae* claims asserted by the States.

The trial court's thorough and analytical Memorandum and Order may be found in *In re Wyoming Tight Sands Antitrust Cases*, 695 F. Supp. 1109 (D. Kan. 1988).

The States sought and obtained interlocutory appellate review of a certified question. The public utilities are the appellees. The defendants are not involved in this appeal. At the request of the States, the question certified to the court pursuant to 28 U.S.C. § 1292(b) is as follows:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

Wyoming Tight Sands, 695 F. Supp. at 1120.

The States now quarrel with the certified question. The States point out that all of the utilities that purchased the alleged price-fixed gas are not present as plaintiffs and assert that *all* of the illegal overcharges were passed on to residential consumers. The utilities assert the proposed modifications to the question are irrelevant to the issues in this appeal, and ask us to disregard the proposed factual allegations and consider the question certified by the district court.

This court will answer the question certified to us by the district court for the reasons contained in the body of this opinion.

II.

The defendant Williams Natural Gas Company is alleged to have transported natural gas from gas fields in Wyoming and sold it to the public utilities. The remain-

ing defendants, being the producers of the natural gas, are alleged to have conspired with Williams Natural Gas Company, the pipeline company, to artificially inflate the price of the natural gas.

The public utilities have sold or used the natural gas purchased from the pipeline company in different ways and therefore occupy different levels in the distribution chain. Kansas Gas & Electric Company purchased gas directly from the pipeline company for use in generating electricity, and the electricity was then sold and delivered to commercial, industrial and residential customers. Kansas Power & Light Company and UtiliCorp United Inc. purchased natural gas directly from the pipeline company for their own industrial use and for delivery to commercial, industrial and residential consumers. All three of the public utilities operate as regulated monopolies within defined service areas.

The trial court made no findings of fact concerning how much of the natural gas overcharges were passed on to the commercial, industrial and residential consumers. The States offered evidence that all the overcharges were passed on to the ultimate consumers. The trial court apparently based its partial summary judgment upon the theory that there was no need to decide whether the allegedly illegal overcharges were passed on in whole or part. The question certified to us states that "most or all" of the price increase was passed on to the consumers.

The states of Kansas and Missouri are bringing two claims. The first relates to direct purchases of natural gas made by the States and its various instrumentalities. This claim is not now before this court. The States' second claim is in its capacity as *parens patriae* on behalf of natural persons residing therein who are residential in-

direct purchasers of natural gas.[1] This is the claim we now decide.

III.

The States acknowledge the basic rule as set forth in *Hanover Shoe*, 392 U.S. 481, and as expanded in *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). These cases hold that only the direct purchaser, and no other in the distribution chain, is the "party injured" within the meaning of § 4 of the Clayton Antitrust Act, 15 U.S.C. § 15. Stated differently, only the direct purchaser may sue for and recover the full amount of the illegal overcharge.

All rules have exceptions, and the basic rule set forth above has at least two, the cost-plus exception and the control exception. The States contend they fall squarely into either or both of these exceptions and should therefore be allowed to proceed with their suits on behalf of the residential consumers. The States, in their joint reply brief, concede the utilities' right to sue for and recover the alleged damages on behalf of the commercial and industrial customers of the utilities.

The first exception to the basic rule is what we have labeled as the cost-plus exception. The genesis of this exception may be found in *Hanover Shoe*. There the Supreme Court recognized that "there might be" an exception to the rule "for instance, when an overcharged

1. It should be noted that §§ 4C through 4H of the Clayton Act, 15 U.S.C. §§ 15c through 15h, which is sometimes described as the Hart-Scott-Rodino Antitrust Improvements Act of 1976, empowers state attorneys general to bring treble-damage actions as *parens patriae* on behalf of resident natural persons "for injury sustained . . . to their property" by reason of any Sherman Act violations. The parties have not argued that this law eliminates the basic rule that only a direct purchaser may sue. We assume that this statutory provision comes into play when the individual consumers are the direct purchasers.

buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." *Id.* at 494. The Supreme Court further elaborated on this exception in *Illinois Brick* when it said:

> *Hanover Shoe* indicated the narrow scope it intended for any exception . . . by citing, as the only example . . . a pre-existing cost-plus contract. In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price.

Id. at 735-36. We interpret this exception as requiring a pre-existing cost-plus contract for a fixed quantity. We also note the Supreme Court did not say this would constitute an exception but rather that it "might be," and for this reason we have narrowly construed the exception as also requiring a fixed quantity.

The States now assert that their system of price regulation of natural gas utilities creates a cost-plus pricing arrangement that, coupled with the residential consumers' need to purchase their full requirements of natural gas from the utilities, places the residential consumers squarely within the cost-plus exception. In making this assertion, the States place great reliance on *State ex. rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.), *cert. denied*, 109 S.Ct. 543 (1988).

Prior to analyzing the States' contentions, we must delve deeper into *Hanover Shoe* and then into *Illinois Brick*, as we can glean several principles therefrom to guide us in deciding this case. The direct purchaser is entitled to damages if he raises the price for his own product. *Hanover Shoe*, 392 U.S. at 489. Considerations of *stare decisis* weigh heavily in the area of statutory con-

struction where Congress is free to change the Supreme Court's interpretation of its language. *Illinois Brick*, 431 U.S. at 736. New dimensions of complexity would be added to treble-damage suits and seriously undermine their effectiveness if massive efforts were made to apportion the recovery among all potential plaintiffs. *Id.* at 737. There exists a serious problem of measuring the change in quantities of the natural gas purchased by consumers in response to a change in price. *Id.* at 742. There should be no exceptions to the basic rule for particular types of markets. *Id.* at 744. The increase in complexity of treble-damage suits will result in a reduction in the effectiveness of these suits. *Id.* at 745. There is a long-standing policy of encouraging vigorous private enforcement of the antitrust laws. *Id.* at 745.

We may distill these principles and summarize them by stating that the reasons given by the Supreme Court to justify its interpretation of the statute in *Hanover Shoe* and *Illinois Brick* are: (1) *stare decisis;* (2) encourage vigorous enforcement of the antitrust laws by reducing the expense of trial by eliminating unnecessary complications; (3) give to the direct purchaser an incentive to discover and prosecute antitrust violations; (4) avoid the problems of apportionment of damages; and (5) exceptions to the basic rule are to be narrow in scope.

First, as to *stare decisis*. *Illinois Brick* contains a message to Congress as well as to students of the law. That message is simple. The phrase "[a]ny person who shall be injured" as used in § 4 of the Clayton Act means only a direct purchaser from the antitrust violator. In short, *stare decisis* requires that when a decision of the Supreme Court is made, it is binding on courts of appeals. In this case, the rule is clear, and the Supreme Court has

cautioned us concerning expansions to the exception. Were we to broadly construe the exceptions, we would also be diluting the clear message given to Congress concerning the Supreme Court's construction of § 4 of the Clayton Act.

Second, as to avoiding adding complexity and expense to antitrust suits. Were we to construe the law to allow the States to pursue their *parens patriae* claims, then unnecessary issues would be added to the trial, including the unresolved factual issue of how much of the alleged illegal overcharge was passed on to the residential consumers of each utility. If all overcharges were passed on, then allowing the consumers to prove and collect the damages could result in the antitrust violators escaping the payment of damages relating to decreased demand by residential consumers due to the higher price. Complex issues of proof will grow geometrically if the States press their consumers' demands, unless we should rule as a matter of law that the utilities' share of the alleged damages are likewise passed on to the consumers. This we are not prepared to do, given the factual record before us. The question certified to us provides that "most or all" of the illegal price increase was passed on.

Third, as to giving the direct purchaser an incentive to discover and prosecute the antitrust violator. It can be argued that enforcement of the antitrust laws would not be imperiled by allowing the States to pursue their claims in this case. But what of the next case? By removing an incentive for a utility to discover and enforce antitrust violations, would we not be shifting the incentive to an indirect purchaser? Would we not be shifting the cost of policing and enforcing the antitrust laws to the states? Would we not be undercutting the basic rationale

for the Supreme Court's decisions in *Hanover Shoe* and *Illinois Brick?* As stated by the Supreme Court in *Hanover Shoe*:

> [A]ntitrust laws will be more effectively enforced by concentrating the full recovery for the overcharge in the direct purchasers rather than by allowing every plaintiff potentially affected by the overcharge to sue only for the amount it could show was absorbed by it.

Id. at 735.

The argument can be made that the utility really has no incentive to sue because the public utility regulatory commission of the state may force the utility to pass on to the consumers all damages the utility may recover. This is a question we do not answer. If is sufficient to state that a utility filed first in this case. It should also be noted that the utilities' motions to strike the pass-on defense asserted by the gas suppliers and transporters was characterized by the trial court as being in reality a motion to strike the States' *parens patriae* claim. It is reasonable to assume that the public utilities must believe there is something for their benefit in pursuing these actions. Allowing the States to press the claims of the indirect purchasers will result in the probability that direct purchasers will fail to discover and aggressively assert antitrust claims.

Fourth, as to apportioning damages. The States assert there is no problem in apportioning the hoped-for damages in this case. They contend that it is a simple matter of proving how much natural gas went to the residential consumers and multiplying this by the unit illegal overcharge. The States may have an overly simplistic view of this problem and may not have considered

the nature of the defenses which will probably be asserted at trial. Any allocation of illegal overcharges to the residential consumers may require tracing the sale from the wellhead through each level of distribution in order to establish the amount of illegal gas costs actually paid by the consumers in each state, probably resulting in exactly that which the Supreme Court prohibited, i.e., adding new dimensions of complexity to antitrust suits. There is no way this court could or would instruct the parties on proof of damages prior to trial as there are too many facts not now known. Suffice it to say that apportioning damages will probably not be as simple as contended by the States.

Looking at the rationales underlying the basic rule, we are of the opinion that to allow the cost-plus exception urged upon us by the States would undercut the very reasons for the basic rule.

Fifth, as to the words of the exception itself. To say that the utilities have a cost-plus fixed fee contract for a fixed quantity with their residential consumers would amount to fitting a square peg into a round hole. There exists no contract between the utilities and their residential consumers for any particular quantity. Obviously a residential consumer could stop using natural gas and convert to an alternative source of energy such as wood or coal, or a consumer could decrease the quantity of natural gas used. The apparent reason for the fixed-quantity requirement to the cost-plus exception is simply that there would exist no problem of apportionment between the direct and indirect purchasers. In this case, the problem of apportionment would exist even if all of the overcharge was passed on, because there still exists the issue of decreased residential demand caused by the

higher price. We hold that suit by residential consumers of natural gas who are not direct purchasers does not lie within the cost-plus exception to the basic rule.

The States urge us to apply the law as enunciated in *Panhandle Eastern*, 852 F.2d 891. This we decline to do.

Panhandle Eastern held, in effect, that the purchased gas adjustment component of gas utility regulation, coupled with the fact that residential consumers are obligated to purchase their full requirements of natural gas from monopolistic utilities, placed the residential consumer squarely within the cost-plus exception of *Hanover Shoe* and *Illinois Brick*.

We distinguish the facts of this case from those in *Panhandle Eastern*. In *Panhandle Eastern*, there was formal cost-plus pricing (as we may have here); a contract that required 100 percent passing on (as we may or may not have here);[2] and an acknowledgment of 100 percent pass-on in every kilowatt-hour resold to the utilities' residential consumers (which we may or may not have here). In *Panhandle Eastern* the utility had delayed in filing suit, and there was a serious question as to whether or not the statute of limitations had expired. In *Panhandle Eastern* the court was dealing with the residential consumers of a single utility; here we are dealing with utilities that occupy different levels on the distribution chain within two states, and with two states and their attendant public utility rate regulation schemes. In this

2. In this case, there is a purchased-gas adjustment clause in the rate tariffs of Kansas Power & Light. There is an energy-cost adjustment clause, which operates in a similar manner, in Kansas Gas & Electric's operating tariff in Kansas. In Lawrence, Kansas, the Kansas Public Service Company, a division of UtiliCorp, did not resell natural gas by way of a purchased-gas adjustment clause mechanism.

case we have yet another unresolved factual issue: UtiliCorp asserts in its brief that more of the allegedly illegal overcharges could be recovered if the utilities were allowed to press the claims of the residential consumers, an assertion which the court in *Panhandle Eastern* apparently did not face. The Seventh Circuit itself stated in *Panhandle Eastern* that this case (*Wyoming Tight Sands,* 695 F. Supp. 1109) was distinguishable from *Panhandle Eastern.* 852 U.S. at 893. The most important difference between *Panhandle Eastern* and this case may be that there was apparently no doubt in *Panhandle Eastern* that the entire overcharge was passed on, and there was no need to apportion damages between the direct and indirect purchasers. In this case, the amount of the overcharge passed on may be an unresolved question of fact. However, even if we assume, as we do for the purpose of deciding the issues before us, that there was a perfect and provable pass-on of the allegedly illegal overcharge, we are not persuaded that the facts of this case would place this case into the narrow exception to the rule. At the most, a perfect pass-on might solve the problem of apportioning damages between the direct and indirect purchaser but for the issue of decreased demand due to higher prices. This does not justify shifting the incentive to prosecute alleged antitrust violations from the direct purchaser, who is the closest to the violator and who presumably has the better knowledge, to the indirect purchaser. A perfect pass-on of all illegal overcharges may exist in a model world but probably does not exist in the real world. A perfect pass-on, standing alone, is not sufficient reason to allow an indirect purchaser to sue an alleged antitrust violation. We narrowly construe the cost-plus exception as to do otherwise would be to do that which the Supreme Court has cautioned against. We

hold the controlling cases are *Hanover Shoe* and *Illinois Brick,* and not *Panhandle Eastern.*

The States also rely upon *In re New Mexico Natural Gas Antitrust Litig.,* 1982-1 Trade Cases ¶ 64,685 (D.N.M. 1982). We distinguish this case, as the direct purchasers were billing their consumers monthly and separately for a "cost of gas component," and perhaps more importantly, the residential consumers constituted the first direct purchasers from the conspiring defendants.

We are not persuaded that the cost-plus contract exception of *Hanover Shoe* is applicable to the facts of this case. If we were to adopt the reasoning of *Panhandle Eastern,* we would in reality be carving out yet another exception (regulation of public utilities) to the basic rule that only a direct purchaser may sue for the antitrust violation, and this we are unwilling to do.

IV.

In *Illinois Brick,* the Supreme Court set forth another situation where the pass-on defense "might be" permitted, and that is where the direct purchaser is owned or controlled by its customer. *Id.* at 736 n.16.

The States argue that as they exercise plenary authority over the utilities, particularly with regard to rates, this fact equates to placing the States within the control exception. We do not agree. As the trial court stated: "The utilities are for-profit, publicly held corporations and simply do not fit within this exception." *Wyoming Tight Sands,* 695 F. Supp. at 1117. Calling a cow a horse does not make it so. State regulation of utility rates does not give to the states or its citizens ownership or control of the public utilities. We hold that the public utilities

in this case are neither owned nor controlled by its customers, and we therefore conclude that the "control exception" does not apply to this controversy.

V.

The States next assert that allowing residential consumers to sue is fully consistent with the prior decisions of this court, citing *Central Nat'l Bank v. Rainbolt*, 720 F.2d 1183 (10th Cir. 1983); *Zinser v. Continental Grain Co.*, 660 F.2d 754 (10th Cir. 1981), *cert. denied*, 455 U.S. 941 (1982); and *Jones v. Ford Motor Co.*, 599 F.2d 394 (10th Cir. 1979). These cases are inapposite. None involves pass-on or cost-plus contracts.

The States next urge that *Illinois Brick* should not be read as a rigid bar to recovery on the part of all indirect purchasers and cite *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982), wherein plaintiff was allowed to maintain an antitrust suit as she was the person who was "out of pocket" by paying her psychologist when Blue Shield was exerting coercive pressure to induce its subscribers into selecting psychiatrists over psychologists, and *Associated Gen. Contractors of California, Inc. v. California State Council of Carpenters*, 459 U.S. 519 (1983), wherein the Supreme Court held that a decision as to antitrust standing requires a case-by-case analysis of at least six factors.

These cases are distinguishable. In *Blue Shield*, the Supreme Court held that plaintiff was in essence the direct purchaser when it stated "it is not the employer as purchaser, but its employees as subscribers, who are out of pocket as a consequence of the plan's failure to pay benefits." *Id.* at 475. The Court held that McCready had paid her psychologist; Blue Shield failed to pay her; and

McCready's psychologist could link no claim of injury to himself arising from his treatment of McCready. In the instant case, the residential user of gas paid the utility and the utility can assert a claim of injury for decreased consumer demand. In *Associated Gen. Contractors*, the Supreme Court applied the policies underlying *Illinois Brick*, and dismissed the claims of a labor union for indirect damages, holding that the union's claim of consequential harm was insufficient as a matter of law. *Id.* at 545.

The States assert that the trial court should not have granted partial summary judgment as there may exist a genuine issue of material fact, i.e., did the utilities pass on all of the overcharges. In *Illinois Brick*, the Supreme Court stated, "[T]he process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid." *Id.* at 744-45. We therefore hold that the amount of illegal overcharges actually passed on by the utilities to its customers is not an issue of material fact necessary to a resolution of the narrow issue before this court.

We conclude that residential indirect purchasers of natural gas are not entitled to sue the alleged violators under either *Hanover Shoe* or *Illinois Brick*. The question certified to us is answered in the negative, and the judgment of the trial court, insofar as is necessary to answer the question certified, is AFFIRMED.

APPENDIX B

(Filed March 27, 1989)

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Nos. 88-2158
88-2159

In Re:

WYOMING TIGHT SANDS ANTITRUST CASES.

THE STATE OF KANSAS, as parens patriae on behalf of natural person residing in Kansas, ROBERT T. STEPHAN, Attorney General of the State of Kansas,

and

STATE OF MISSOURI,
Plaintiffs-Appellants,

KANSAS POWER & LIGHT COMPANY, a Kansas Corporation, KANSAS GAS & ELECTRIC COMPANY,
Plaintiffs-Appellees,

UTILICORP UNITED INC.,
Plaintiff-intervenor-Appellee,

v.

AMOCO PRODUCTION CO., CITIES SERVICE OIL AND GAS CORPORATION, f/k/a Cities Service Company, CSG EXPLORATION COMPANY, WILLIAMS NATURAL GAS COMPANY, f/k/a Northwest Central Pipeline Corporation, THE WAMSUTTER LIMITED PARTNERSHIP, THE MOXA LIMITED PARTNERSHIP,
Defendants-Appellees.

ORDER

Before Holloway, McKay, Seymour, Moore, Tacha, Baldock, and Brorby, Circuit Judges.

This matter comes on for consideration of appellants' joint petition for rehearing and suggestion for rehearing en banc.

Upon consideration whereof, the petition for rehearing is denied by the panel to whom the case was argued and submitted.

In accordance with Rule 35(b) of the Federal Rules of Appellate Procedure, the petition for rehearing and suggestion for rehearing en banc were transmitted to all the judges of the court in regular active service. No member of the hearing panel and no judge in regular active service on the court having requested that the court be polled on rehearing en banc, Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing en banc is denied.

Judges Logan, Anderson and Ebel did not participate.

Entered for the Court

Robert L. Hoecker
Clerk
By: /s/ Patrick Fisher
Patrick Fisher
Chief Deputy Clerk

(Filed April 6, 1989)

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

JANUARY 31, 1989.

Before the Honorable Stephanie K. Seymour, Honorable John P. Moore and Honorable Wade Brorby, Circuit Judges.

Nos. 88-2158
88-2159
(D.C. Lead No. CIV 85-2349-S)

In re

WYOMING TIGHT SANDS ANTITRUST CASES.

STATE OF KANSAS, as parens patriae on behalf of natural person residing in Kansas, ROBERT T. STEPHAN, Attorney General of the State of Kansas,

and

STATE OF MISSOURI,
Plaintiffs-Appellants,

KANSAS POWER & LIGHT COMPANY, a Kansas Corporation; KANSAS GAS & ELECTRIC COMPANY,
Plaintiffs-Appellees,

UTILICORP UNITED INC.,
Plaintiff-intervenor-Appellee.

v.

AMOCO PRODUCTION CO.; CITIES SERVICE OIL AND GAS CORPORATION, f/k/a Cities Ser-

vice Company; CSG EXPLORATION COMPANY; WILLIAMS NATURAL GAS COMPANY, f/k/a Northwest Central Pipeline Corporation; THE WAMSUTTER LIMITED PARTNERSHIP; THE MOXA LIMITED PARTNERSHIP,
Defendants-Appellees.

JUDGMENT

This cause came on to be heard on the record on appeal from the United States District Court for the District of Kansas, and was argued by counsel.

Upon consideration whereof, it is ordered that the judgment of that court is affirmed.

ROBERT L. HOECKER
Clerk
By /s/ Patrick Fisher
Patrick Fisher
Chief Deputy Clerk

APPENDIX C

(Filed May 4, 1988)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

CIVIL ACTION NO. 85-2349-S
& CONSOLIDATED CASES

IN RE

WYOMING TIGHT SANDS
ANTITRUST CASES

MEMORANDUM AND ORDER

These consolidated actions concern allegations that certain suppliers of natural gas conspired to fix inflated prices in violation of the federal antitrust laws. Several distinct categories of plaintiffs are suing several distinct categories of defendants. The issue presently before the court is ultimately one of standing: Who are the proper parties to assert the antitrust claims?

I.

The facts can be simplified for purposes of the present dispute. Three companies (defendants Amoco Production Company, CSG Exploration Company, and Cities Service Oil and Gas Corporation) and two limited partnerships formed by the companies (defendants Moxa Limited Partnership and Wamsutter Limited Partnership) produced natural gas out of the Wyoming Tight Sands formation in the State of Wyoming. The companies, through the limited partnerships, contractually committed certain amounts

of natural gas to the successors of defendant Williams Natural Gas Company (Cities Service Gas Company (CSGC), and Northwest Energy Company (NWC)), which operated an interstate pipeline and which had an affiliation with CSG. *See generally Midwest Gas Users Ass'n v. FERC*, 833 F.2d 341, 345-49 & nn. 3-5 (D.C. Cir. 1987) (discussing the background of the various actors in this controversy). The allegation is that these six entities (the three producing companies, two producing limited partnerships, and the pipeline) conspired to inflate prices.

The plaintiffs represent several vertical levels in relation to the pipeline. Farmland Industries, Inc. is an agricultural concern that purchased gas directly from the pipeline for its own consumption. Kansas Gas and Electric (KG&E) is a public utility that purchased gas directly for use in generating electricity, which was then delivered to industrial and residential consumers. Kansas Power and Light Company (KP&L) and Utilicorp United, Inc. (Utilicorp) are public utilities that purchased gas directly from the pipeline for their own industrial use and for delivery to industrial and residential consumers. The States of Kansas and Missouri have asserted two types of claims: (1) On behalf of residential consumers who purchased gas from the utilities, the States are in this lawsuit in a *parens patriae* capacity; and (2) On behalf of state agencies, municipalities, and other political subdivisions that purchased gas directly from the pipeline, the States are suing in a representative capacity. *See* Appendix to this Memorandum and Order (charting the vertical and horizontal relationships of the parties). The damages asserted by all plaintiffs arise from the allegedly illegal inflation of the price of natural gas. All plaintiffs seek reimbursement for the overcharge (along with the treble damage award in 15 U.S.C. § 15), with the utilities also alleging

that the illegally inflated price of natural gas caused a decrease in consumer consumption and a corresponding decrease in profits. The utilities contend that because their rates are regulated, their profits are directly related to consumer demand.

Plaintiffs KG&E and KP&L and plaintiff-intervenor Utilicorp have moved to strike certain defenses or, in the alternative, for partial summary judgment. The defenses they seek to strike deal with the "pass-on" theory of avoiding antitrust liability. Section 4 of the Clayton Act grants certain persons standing to bring an antitrust lawsuit:

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained . . . .

15 U.S.C. § 15 (1982). Defendants Cities Service Oil & Gas Corporation, GSG Exploration Company, Amoco Production Company, and Williams Natural Gas Company have asserted numerous defenses, including allegations that the public utility plaintiffs (1) lack standing under Section 4 and (2) have not been injured in their business or property under Section 4. These defendants allege that the utilities have passed on dollar-for-dollar any illegal increase in the price of natural gas, so that the consumer has borne the entire cost of any antitrust injury. This is the "pass-on" defense. The United States Supreme Court has abolished the pass-on theory, with several narrow exceptions. Defendants assert that these exceptions apply in this case.

II.

In *Hanover Shoe, Inc. v. United Shoe Mach. Corp.*, 392 U.S. 481 (1968), a manufacturer of shoes sued a manufacturer and distributor of shoe machinery for violations of the Sherman Act, 15 U.S.C. § 4, alleging that the latter's practice of leasing and refusing to sell its more complicated and important shoe machinery was an instrument of unlawful monopolization. 392 U.S. at 483. United Shoe Machinery, the machine manufacturer, claimed that plaintiff Hanover Shoe suffered no legally cognizable injury, because the illegal overcharge was allegedly reflected in the price of Hanover's shoes, so that the consumer suffered the actual monetary injury. The court did not dispute the premise of this argument, but it found that Hanover Shoe was nevertheless entitled to bring the damage action:

> We hold that the buyer is equally entitled to damages if he raises the price for his product. As long as the seller continues to charge the illegal price, he takes from the buyer more than the law allows. At whatever price the buyer sells, the price he pays the seller remains illegally high, and his profits would be greater were his costs lower.

Id. at 489. The Court noted with approval a line of cases in which the possibility that a plaintiff had recouped the overcharges from its customers was found to be irrelevant in assessing damages. *Id.* at 490. As an example of such a situation, the Court discussed a case in which it was alleged that a shipper of goods should not recover in an antitrust lawsuit against a common carrier railroad because the shipper is able to simply pass on to its customers an illegally high charge:

"The general tendency of the law, in regard to damages at least, is not to go beyond the first step. As it does not attribute remote consequences to a defendant so it holds him liable if proximately the plaintiff has suffered a loss. The plaintiffs suffered losses to the amount of the verdict when they paid. Their claim accrued at once in the theory of the law and it does not inquire into later events. . . . The carrier [*i.e.*, the railroad] ought not to be allowed to retain his illegal profit, and the only one who can take it from him is the one that alone was in relation with him, and from who the carrier took the sum. . . . Probably in the end the public pays the damages in most cases of compensated torts."

Id. at 490-91 n.8 (quoting *Southern Pac. Co. v. Darnell-Taenzer Lumber Co.*, 245 U.S. 531, 533-34 (1918)). *See also Associated General Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 519, 534 & n.30 (1983). This analysis is particularly appropriate in the present case, because the utilities have been analogized as being mere shippers or transporters of natural gas from the wellhead to the consumer.

The *Hanover Shoe* Court did recognize at least one possible exception to the unavailability of the pass-on defense—"when an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." 392 U.S. at 494. In so stating, the Supreme Court appeared to be referring to a discussion earlier in the opinion, in which the court justified elimination of the pass-on defense based on the "insurmountable" task of making a convincing showing on each element necessary to establish the applicability of the defense. The elements of the defense were: (1) The buyer

raised his price in response to, and in the amount of, the overcharge; (2) The buyer's margin of profit and total sales had not thereafter declined; and (3) The buyer could not or would not have raised his prices absent the overcharge or maintained the higher price had the overcharge been discontinued. 392 U.S. at 493. The only foreseeable instance in which these elements could be established would have been a fixed quantity, cost-plus contract, thereby creating the exception.

The other major Supreme Court opinion involving the pass-on defense was *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). The ultimate holding of the *Illinois Brick* Court was that the *Hanover Shoe* analysis, which established the unavailability of the pass-on defense to a monopolizing manufacturer in a case brought by a direct purchaser-middleman, applies equally to an indirect purchaser-consumer who attempts to use the pass-on theory offensively by asserting that he has suffered the antitrust injury because the direct purchaser has passed on the entire illegal price increase. While the holding is certainly relevant to the present facts, of equal importance is the Court's interpretation and application of *Hanover Shoe*, along with an explanation of the scope of the exceptions to the general rule.

The defendants in *Illinois Brick* were manufacturers and distributors of concrete block. Their principal buyers were masonry contractors, who submitted bids to general contractors for the masonry portions of construction projects. In turn, the general contractors submitted bids for the overall construction project to customers such as the State of Illinois and its political subdivisions. The State of Illinois, on behalf of in itself and its political subdivisions, filed an antitrust action against the defendants,

alleging that the latter had engaged in a combination and conspiracy to fix prices in violation of section 1 of the Sherman Act, 15 U.S.C. § 1. If all or part of the illegal overcharge was passed on by the masonry and general contractors to the plaintiffs, then seemingly the plaintiffs had been "injured in [their] person or property" under section 4 of the Clayton Act. 431 U.S. at 726-27.

The *Illinois Brick* Court reemphasized both the basic principle that the pass-on theory is not available in antitrust litigation and the limited role that any exception could be allowed to play. The Court acknowledged two possible exceptions. The first was the *Hanover Shoe* cost-plus exception:

> In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price. The effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand that complicates the determination in the general case.

431 U.S. at 736.* As for the second, the Court noted in a footnote that "[a]nother situation in which market forces

*At least one federal judge has attempted to minimize the requirement that a contract under this exception must be of fixed quantity. In *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206, 1210 (7th Cir. 1988) (Posner, J., dissenting in part), Judge Posner questioned whether the reference in *Illinois Brick* to "fixed quantity" was intended to state an independent requirement of the cost-plus exception or merely to describe a normal contract situation. *Id.* at 1211. As the majority in *Panhandle Eastern* noted, the *Illinois Brick* Court "regarded the predetermination of quantity as an essential element of the exception." *Id.* at 1209. Furthermore, as earlier discussed in this opinion, the *Hanover Shoe* Court originally imposed as an element of the pass-on defense a showing that

(Continued on following page)

have been superseded and the pass-on defense might be permitted is where the direct purchaser is owned or controlled by its customer," *id.* at 736 n.16, although the Court did not explain the parameters of the "control" necessary to fall within this exception.

The *Illinois Brick* Court expressly considered permitting several vertical levels of injured persons to bring one lawsuit against the alleged wrongdoers (*i.e.*, as in the present case with direct and indirect purchasers), a seemingly logical, efficient, and fair way to allocate the totality of damages suffered as a result of antitrust activity. The allure of this procedure did not impress the Supreme Court:

> Permitting the use of pass-on theories under § 4 essentially would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge—from direct purchasers to middlemen to ultimate consumers. However appealing this attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness.

431 U.S. at 737. The Court's subsequent discussion of the difficult economic analyses that would have to be introduced in a case involving several levels of purchasers dis-

Footnote continued—

total sales had not declined as a result of the increase in price precipitated by illegal antitrust activity. Both *Illinois Brick* and *Hanover Shoe* permit assertion of the pass-on defense only when the ultimate demand by consumers is perfectly inelastic—as in the case of existing fixed-quantity contracts—because of the "serious problems" in measuring the relative elasticities of demand. *Illinois Brick*, 431 U.S. at 742; *Hanover Shoe*, 392 U.S. at 493.

plays some fears that admittedly would not be present under the facts of this case. For instance, the Court noted the possibly incalculable effect that imperfectly competitive markets might have on the determination of damages, such as when direct purchasers compete with sellers who have not been subject to the overcharge. Of course, in the public utility area, the complete lack of competition eliminates this problem. The fact that the alleged antitrust activity took place in the context of a public utility direct purchaser renders inapplicable much of the rationale behind the decisions in *Illinois Brick* and *Hanover Shoe*, both of which involved manufactured goods in the free market. Moreover, the concern that the plaintiff's damages be proximately caused by the kind of antitrust activity that Congress contemplated in section 4, as expressed by a subsequent Supreme Court opinion, is significantly allayed in this case, where *the fact* of actual monetary injury to residential consumers of natural gas caused by the alleged price fixing is easily established. *See Associated General Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 465, 535-45 (1983) (discussing the requirement of proximate cause). Nevertheless, the Supreme Court recognized the inevitability of a case involving less complicated factual difficulties and endeavored to make the general rule as pervasive as possible:

> It is quite true that these difficulties and uncertainties will be less substantial in some contexts than in others. There have been many proposals to allow pass-on theories in some of these contexts while preserving the *Hanover Shoe* rule in others. . . .
>
> We reject these attempts to carve out exceptions to the *Hanover Shoe* rule for particular types of markets. . . .

> [T]he process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid. The litigation over where the line should be drawn in a particular class of cases would inject the same "massive evidence and complicated theories" into treble-damages proceedings, albeit at a somewhat higher level of generality.

431 U.S. at 743-45.

In *Illinois Brick*, the Court certainly considered that by instituting direct purchasers as the injured parties with standing in an antitrust suit, some indirect purchasers who have suffered identifiable antitrust injury might be left uncompensated. The Court did not believe this to be sufficient enough to overcome the other factors supporting the *Hanover Shoe* rule. *Id.* at 745-47. This demonstrates the extreme lengths to which the Court was willing to go in simplifying the already complex nature of an antitrust lawsuit.

The Supreme Court has issued several subsequent opinions concerning the proper plaintiff in an antitrust action. *See Associated General Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 519 (1983); *Blue Shield of Va. v. McCready*, 457 U.S. 465 (1982). In *McCready*, the plaintiff was a beneficiary under an employer-sponsored health plan. The plan followed a practice of reimbursing the costs of psychotherapy administered by psychiatrists but not by psychologists. Plaintiff was treated by a psychologist, and the plan denied her claim for reimbursement. The Court held that

the plaintiff had standing to bring an antitrust lawsuit against the plan, but it found the policies of *Illinois Brick* inapplicable because in *McCready*, the plaintiff had suffered *direct* injury by the plan's refusal to pay her. 457 U.S. at 474-75. In *Associated General Contractors*, the Court found that a union does not have standing in an antitrust lawsuit brought against certain companies that induced landowners not to hire union contractors. In such a case, the coerced landowners or the union contractors have suffered the direct injury. 459 U.S. at 540-42. The case is consistent with *Illinois Brick* and relied substantially on its analysis. 459 U.S. at 543-45.

Having reviewed the relevant Supreme Court authority on the issue, the court will turn to the arguments of the parties and how they fit in the scheme of the cases discussed above.

III

First, plaintiffs States of Kansas and Missouri and the defendants [hereinafter referred to as "the opposing parties"] argue that the utilities' motions are inappropriate because there has not been sufficient discovery in this litigation to fully disclose all possible factual issues. These cases were filed in 1985 and it is now 1988. The court does not intend to permit this litigation to drag on indefinitely. Furthermore, the court will not withhold disposition of the motions to strike or for partial summary judgment based on a possible or speculative issue of fact which the opposition has yet to determine. If the utilities can demonstrate the existence of all necessary, uncontroverted facts, there is no legal justification in withholding judgment, whether discovery has proceeded for twenty days or twenty years.

Along this same vein, the opposing parties ask the court to defer ruling on the issue because if facts or the law subsequently develop such that dismissed parties must be brought back into the litigation, the remaining parties will be prejudiced. The court believes that if the current state of the law requires dismissal, it would be inappropriate to defer a ruling based again on a possible change in the law or in the course of the litigation.

The principal alleged unestablished factual issue is whether the utilities passed on the entirety of any allegedly illegal overcharge. The opposing parties contend that if the facts establish that the rate systems governing the utilities permitted a total pass-through of any price increase (provisions titled "energy cost adjustment" or "purchased gas adjustment"), the arrangement would constitute the functional equivalent of the "cost-plus" contract exception recognized by *Hanover Shoe*. The parties appear to be asking for a "perfect pass-on" exception to the *Hanover Shoe* "no pass-on" rule. The argument for which the opposing parties now request additional discovery is precisely the argument that the Supreme Court overruled in *Hanover Shoe*. The Court expressly considered the situation in which a direct purchaser has passed on the *entire* illegal overcharge, and it rejected any dispositive effect this fact would have. 392 U.S. at 489-91 & n.8. Other federal court decisions have recognized this and similarly held an absolute passing-on of an overcharge not to be dispositive. *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line*, 839 F.2d 1206, 1209 (7th Cir. 1988) ("[T]here could be a 'functional equivalent' of a cost-plus contract for a fixed quantity only where factors . . . made inevitable an exact passing on of price variation *applied to a predetermined quantity* . . . .) (emphasis added); *Carter v. Berger*, 777 F.2d 1173, 1175 (7th Cir.

1985) ("[T]he direct purchaser recovers from the wrong-doer the full overcharge, trebled, even if it also recovered the whole overcharge by raising its own prices."). The court does not believe it necessary to wait upon evidence establishing the degree to which the utilities passed on the overcharge, when the Supreme Court has already disregarded its impact. In fact, under the Supreme Court's analysis, the only factual issue that would have relevance here is whether the delivery of natural gas to consumers was made pursuant to fixed quantity contracts. However, both sides agree that consumer demand for natural gas is governed neither by a fixed-quantity contract nor by anything resembling its "functional equivalent."

Besides the cost-plus contract exception, the parties opposing the present motions have attempted to assert several other exceptions. The first is the control exception noted by the Supreme Court in *Illinois Brick*: An indirect purchaser is a proper party when the direct purchaser is owned or controlled by its customer (or vice versa, as other federal courts have held). The Sixth Circuit has read this exception as being limited to relationships "involving such functional economic or other unity between the direct purchaser and . . . the defendant . . . that there effectively has been only one sale." *Jewish Hosp. Ass'n v. Stewart Mechanical Enter., Inc.*, 628 F.2d 971, 975 (6th Cir. 1980), *cert. denied*, 450 U.S. 966 (1981). The court does not believe that even a colorable claim can be made to economically tie these public utilities so closely to residential consumers that the relationship is within that contemplated by the Supreme Court. The utilities are for-profit, publicly held corporations and simply do not fit within this exception.

The second exception asserted by the opposing parties, and one that has not been addressed by the Supreme

Court, is not really an "exception" at all. The theory is that when the direct purchaser participated in the allegedly illegal activities, the indirect purchaser would be the proper plaintiff. Of course, if a direct purchaser utility has participated in antitrust activity, it should be a named defendant just as the pipeline company is in the present case. In such a situation, residential and industrial consumers would become the "direct purchasers" for purposes of the *Hanover Shoe* analysis, because they would be the first purchasers outside the conspiracy. They would not be considered "indirect purchasers" at all. Clearly, all parties in the present litigation are operating under the premise that the utilities hold the status of "direct purchasers," although the predecessors of Williams Natural Gas Company were in fact the first purchasers of natural gas from the producers. Because the pipeline company is alleged to have participated in the conspiracy, the utilities are considered the direct purchasers. The court has been shown no credible evidence that the utilities were part of the antitrust conspiracy in this case, nor has any such claim been filed in this suit. Therefore, the co-conspirator theory is inapplicable.

The opposing parties' arguments have failed to convince this court of the inapplicability of *Hanover Shoe* and *Illinois Brick*. It is not a result of irrational, dogmatic adherence to precedent that this is so. There are principled reasons why the pass-on defense should not be permitted in this case. For example, the Supreme Court recognized that a goal of the antitrust laws is compensating the victims of antitrust activity. *Illinois Brick*, 431 U.S. at 746. In fact, in his dissent from *Illinois Brick*, one of Justice Brennan's main concerns was that by denying the pass-on defense, "[i]njured consumers are precluded from recovering damages from manufacturers." *Id.* at 749

(Brennan, J., dissenting). However, any recovery by the utilities in this case will be passed on in substantial part to the consumers. The ratemaking authorities adjust the utilities' charges after considering all sources of income and expense. If the utilities prevail on their antitrust claim, their recovery will be passed on to the consumers either through a reduction in prices or through a rebate. This appears to be an eminently fair and efficient means of apportioning any damage award, much more so than through protracted litigation.

Additionally, the Supreme Court expressed concern that by including indirect purchasers, the ensuing "massive and complex damages litigation not only burdens the courts, but also undermines the effectiveness of treble-damages suits." *Associated General Contractors*, 459 U.S. at 545. Moreover, the participation of indirect purchasers "would increase the overall costs of recovery by injecting extremely complex issues into the case." *Illinois Brick*, 431 U.S. at 745. Regardless of the opposing parties' representations that disposing of the pass-on defense would not affect the complexity of the litigation, the court believes that the more focused the issues become, the less time and expense this litigation will produce, ultimately benefitting all interests. The residential consumer will receive a greater benefit if attorney's fees and costs are held to a minimum.

The court is by no means going out on a limb in confirming the applicability of *Hanover Shoe* to these facts. Just recently the Seventh Circuit came to the same conclusion on almost identical facts. In *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206 (7th Cir. 1988), the court agreed that in a case involving a public utility which asserted an antitrust claim against a natural gas pipeline, many of the Supreme Court's con-

cerns in *Hanover Shoe* and *Illinois Brick* were not as prevalent, such as the avoidance of multiple recoveries or the complexity of an economic determination of damages. The court held, however, that "*Illinois Brick* did not . . . leave it to the discretion of the lower courts to expand the exceptions to include situations within some range of approximation of the exceptions defined in *Illinois Brick*." *Id.* at 1210. This court agrees with the analysis and decision in *Panhandle Eastern*.

For the reasons outlined above, the court finds that partial summary judgment is proper on the pass-on defense. In so finding, the court does not intend to determine the validity of a standing defense or other defense which relies on an allegation that any damages have not been the result of the type of antitrust injury contemplated by the statute, or a defense that the defendants have not engaged in antitrust activity. The court only holds that the defendants may not use the pass-on defense in arguing that any injury produced by the alleged activity has been passed through to residential and industrial consumers.

The court also is not inclined to grant Utilicorp's other requests to strike. To the extent that any defense raised by defendants is inapplicable to Utilicorp or any other plaintiff, the court directs defendants to clear up their positions in the final pretrial order. If at that time defendants persist in asserting defenses that any of the plaintiffs find inapplicable, an additional motion for summary judgment may be filed.

IV.

The result reached by the court presents a problem as to the status of the States of Missouri and Kansas. The

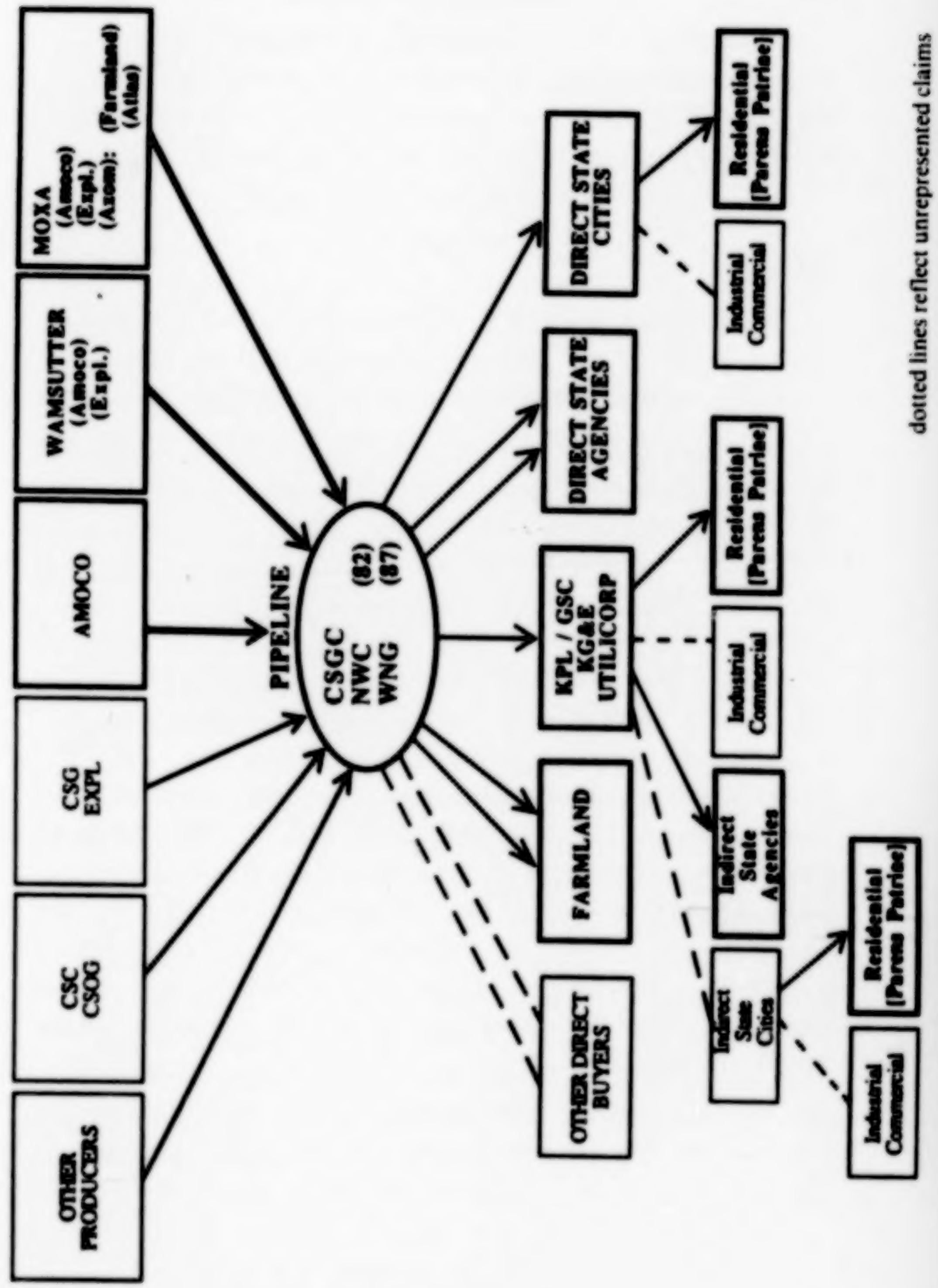
court has determined that the utilities are the proper parties to assert the antitrust claim relating to natural gas delivered to residential consumers, if indeed any compensable antitrust injury has been incurred. While it may be true that the residential consumers represented by the States have suffered actual tangible injury, "[a] showing of antitrust injury is necessary, but not always sufficient, to establish standing under § 4, because a party may not be a proper plaintiff under § 4 for other reasons." *Cargill, Inc. v. Monfort of Colo., Inc.*, 93 L. Ed. 2d 427, 436 n.5 (1986). Having determined that the treble damage remedy is not afforded to residential and industrial indirect purchasers, these persons do not have standing in this lawsuit. Dismissal of these claims need not await further briefing, because all participants in this lawsuit have recognized that the utilities' motions were, in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity. Therefore, the court will dismiss the *parens patriae* claims asserted by the States of Kansas and Missouri.

IT IS BY THE COURT THEREFORE ORDERED that plaintiffs Utilicorp, KG&E, and KP&L's motions for partial summary judgment be granted solely on the pass-on defense. IT IS FURTHER ORDERED that plaintiffs' motions to strike be denied. IT IS FURTHER ORDERED that the claims of the States of Kansas and Missouri as *parens patriae* for their citizens who purchased natural gas from a public utility be dismissed for lack of standing.

DATED: This 4th day of May, 1988, at Kansas City, Kansas.

/s/ Dale E. Saffels
Dale E. Saffels
United States District Judge

APPENDIX



APPENDIX D

(Filed June 7, 1988)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

CIVIL ACTION NO. 85-2349-S &
CONSOLIDATED CASES

IN RE

WYOMING TIGHT SANDS ANTITRUST CASES

MEMORANDUM AND ORDER

On May 4, 1988, the court issued a Memorandum and Order effectively disposing of the States of Kansas and Missouri's *parens patriae* claims in the above-captioned litigation. In support of the decision, the court cited *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206 (7th Cir. 1988). The States of Kansas and Missouri now represent to the court that the opinion in *Panhandle Eastern* has been withdrawn and a motion for rehearing en banc has been granted. The States ask this court alternatively to (1) vacate and rehear or reconsider the opinion of May 4, (2) designate the order as final and appealable under Federal Rule of Civil Procedure 54(b), or (3) certify the issue to the Tenth Circuit Court of Appeals pursuant to 28 U.S.C. § 1292(b). Plaintiffs Utilicorp and KP&L would oppose reconsideration but would acquiesce in an order under 54(b) or 1292(b).

The court finds certification under 1292(b) to be appropriate in this situation. That statute states in relevant part:

> When a district judge, in making in a civil action and [sic] order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order.

The May 4 Memorandum and Order is not otherwise appealable, because it resolves less than all the claims of less than all the parties, and the court is not inclined to permit interlocutory appeal under Rule 54(b). Furthermore, as is evident from the court's order and from the recent action of the Seventh Circuit, the legitimacy of a *parens patriae* claim in this litigation is certainly an area of dispute to which the Tenth Circuit has not spoken. This issue controls several claims of Kansas and Missouri, and an immediate appeal could avoid the possibility of having to conduct two trials in this extremely complex litigation. The facts of this case present precisely the type of situation contemplated by Congress in section 1292(b).

Therefore, the court will certify the following question to the Tenth Circuit Court of Appeals:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

Pursuant to 28 U.S.C. § 1292(b), this certification shall not stay the proceedings in this court.

IT IS BY THE COURT THEREFORE ORDERED that the States of Kansas and Missouri's joint motion for certification pursuant to 28 U.S.C. § 1292(b) be granted; IT IS FURTHER ORDERED that all other requested relief be denied.

DATED: This 7th day of June, 1988, at Kansas City, Kansas.

/s/ Dale E. Saffels
Dale E. Saffels
United States District Judge

APPENDIX E

STATE OF ILLINOIS ex rel. Neil F. HARTIGAN, Attorney General of the State of Illinois, in its proprietary capacity, in its *parens patriae* capacity, and in its representative capacity, Plaintiff-Appellee,

v.

PANHANDLE EASTERN PIPE LINE COMPANY,
Defendant-Appellant.
No. 85-2601.

United States Court of Appeals,
Seventh Circuit.

Argued Feb. 28, 1986.
Decided Jan. 22, 1988.
Rehearing En Banc May 26, 1988.
Decided July 18, 1988.

State brought antitrust action on behalf of consumers of natural gas provided by distributor against interstate supplier of gas seeking damages as result of overcharges. The United States District Court for the Central District of Illinois, Michael M. Mihm, J., denied supplier's motion to dismiss, and supplier sought permission to appeal. The Court of Appeals, Fairchild, Senior Circuit Judge, 839 F.2d 1206, reversed. The full court granted rehearing en banc. On rehearing, the Court of Appeals, Posner, Circuit Judge, held that: (1) state could maintain antitrust suit on behalf of residential consumers of gas under cost-plus exception to general rule prohibiting actions by indirect purchasers, and (2) state could not maintain antitrust action for damages on behalf of industrial customers.

Affirmed in part and reversed in part.

Cudahy, Circuit Judge, concurred and filed opinion.

Fairchild, Senior Circuit Judge, concurred in part, dissented in part, and filed opinion in which Bauer, Chief Judge, and Cummings and Manion, Circuit Judges, joined.

1. Monopolies (Key) 28(1, 6)

State could maintain antitrust suit on behalf of residential consumers of gas distributor against gas supplier alleged overcharging of distributor under cost-plus exception to general rule prohibiting actions by indirect purchasers for supplier's alleged overcharging of distributor; residential customers had cost-plus pricing with direct purchaser, and that pricing was imposed by public utility regulation.

2. Monopolies (Key) 28(1.6)

State could not maintain antitrust action for damages on behalf of industrial customers of gas distributor against gas supplier for supplier's alleged overcharging of distributor, where full amount of any overcharge was not passed on to industrial customers.

Paul H. LaRue, Chadwell & Kayser, Ltd., Chicago, Ill., for defendant-appellant.

Richard L. Miller, Burke & Smith, Chtd., Chicago, Ill., for plaintiff-appellee.

Before BAUER, Chief Judge, CUMMINGS, CUDAHY, POSNER, COFFEY, FLAUM, RIPPLE, MANION, and KANNE, Circuit Judges, and FAIRCHILD, Senior Circuit Judge.*

POSNER, Circuit Judge.

*Circuit Judges WOOD, Jr. and EASTERBROOK did not participate in the consideration or decision of this case.

Central Illinois Light Company (CILCO) is a publicly regulated retail distributor of natural gas. It bought natural gas from Panhandle Eastern Pipe Line Company at prices allegedly inflated because of violations of the antitrust laws by Panhandle, and resold the gas to residential and industrial consumers. In its resales to residential consumers, CILCO passed on the entire overcharge in the form of higher rates. In 1984 the State of Illinois brought this federal antitrust suit on behalf of CILCO's customers against Panhandle—which moved to dismiss the suit as barred by the "indirect purchasers" rule of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 88 S.Ct. 2224, 20 L.Ed.2d 1231 (1968), and *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 97 S.Ct. 2061, 52 L.Ed.2d 707 (1977). The district court denied the motion, but certified its order of dismissal for an immediate appeal under 28 U.S.C. § 1292(b), and we agreed to hear the appeal. A panel of this court reversed the district court and directed it to dismiss the complaint. 839 F.2d 1206 (7th Cir.1988). The full court granted rehearing en banc to decide whether regulatory cost-plus pricing can ever be excepted from the rule that "indirect purchasers" (CILCO's customers are indirect purchasers from Panhandle, CILCO being the direct purchaser) are barred from obtaining antitrust damages from their indirect seller. While the appeal was pending in this court, the district judge conducted a 13-week trial on liability, but he has deferred making a decision until we decide the appeal.

In *Hanover Shoe* the Supreme Court held that it is not a defense to an antitrust damages action that a buyer forced to pay a higher price because of the seller's antitrust violation passed on the cost of the violation to the buyer's customers (the seller's indirect purchasers) by raising his prices to them, unless the buyer had a cost-plus

contract with these customers. *Illinois Brick* announced a corollary to *Hanover Shoe*: the indirect purchaser cannot sue to recover the part of the overcharge that the buyer passed on to him. The Court again recognized an exception for the cost-plus contract, noting that it insulates the direct purchaser from "any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." *Id.* at 736, 97 S.Ct. at 2069-70. Fastening on the words "fixed quantity," the panel majority in this case held that the cost-plus exception is never available when the indirect purchasers are free to vary the quantity they buy from the direct purchaser. The question for decision today is whether the exception is as confined as the panel thought.

The panel's opinion was not the first to read the exception so narrowly. See *Mid-West Paper Products Co. v. Continental Group, Inc.*, 596 F.2d 573, 577 n. 9, 580 (3d Cir.1979); *In re Midwest Milk Monopolization Litigation*, 730 F.2d 528, 533 (8th Cir.1984); *Lefrak v. Arabian American Oil Co.*, 487 F.Supp. 808, 819 (E.D.N.Y. 1980); cf. *Arizona v. Shamrock Foods Co.*, 729 F.2d 1208, 1212 n. 2 (9th Cir.1984); but see *In re Uranium Antitrust Litigation*, 552 F.Supp. 518 (N.D.Ill.1982). And its reading was followed in *In re Wyoming Tight Sands Antitrust Cases*, No. 85-2349-S (D.Kan. May 4, 1988). Yet it was not dictated by precedent. Not only had the prior cases all involved privately negotiated cost-plus contracts rather than cost-plus contractual provisions required by public utility regulation, but there was no reason to believe that the reference to "fixed quantity" in the Supreme Court's opinion in *Illinois Brick* was intended to govern cases so remote from the actual arrangements under scrutiny in that case. The case did not involve a fixed-quantity contract; indeed,

it did not involve a cost-plus contract, but merely an argument (which the Court rejected, see 431 U.S. at 744, 97 S.Ct. at 2074) that a buyer's practice of rule-of-thumb cost-plus pricing should be enough to allow his customers to sue the seller. Certainly there is no indication that by using the words "fixed quantity" the Supreme Court meant to address the issue of the status of regulatory cost-plus pricing. We do a disservice to the Court by wrenching its words out of context and giving them a talismanic significance; we make language a trap rather than a mode of communication. The Supreme Court has never adverted to the issue involved in the present case, and we must consider that issue in relation to the rationale of *Illinois Brick* rather than to isolated phrases in the Court's opinion. If we are to play the language game to which Panhandle invites us, moreover, then we must consider isolated phrases in other Supreme Court opinions, notably the majority opinion in *Blue Shield of Virginia v. McCready*, 457 U.S. 465, 474-75, 102 S.Ct. 2540, 2545-46, 73 L.Ed.2d 149 (1982), where the concern behind *Hanover Shoe* and *Illinois Brick* is described as "the risk of duplicative recovery engendered by allowing every person along a chain of distribution to claim damages arising from a single transaction that violated the antitrust laws." There is, as we shall see, no such risk in this case, at least so far as the residential purchasers from CILCO are concerned; and it is only they who have, in our view, a persuasive claim to be entitled to sue.

Although several district courts have rejected an exception for cost-plus rate regulation, see (besides *Tight Sands*) *Go-Tane Service Stations, Inc. v. Ashland Oil, Inc.*, 508 F.Supp. 200, 204 (N.D.Ill.1981); *City of Cleveland v. Cleveland Electric, Illuminating Co.*, 538 F.Supp. 1320, 1323-27 (N.D.Ohio 1980); *U.S. Oil Co. v. Koch Refining*

Co., 518 F.Supp. 957, 962-63 (E.D.Wis.1981), the cases are distinguishable; and in the case with facts most like those of the present case the court held that indirect purchasers could sue because public utility regulation had created "a straight cost passthrough." *In re New Mexico Natural Gas Antitrust Litigation*, 1982-1 Trade Cases ¶ 64,685, at p. 73,722 (D.N.Mex.1982) [available on WESTLAW, 1982 WL 1827]. Cf. *County of Oakland v. City of Detroit*, 628 F.Supp. 610, 613 (E.D.Mich.1986); *Illinois v. Borg, Inc.*, 548 F.Supp. 972, 975-76 (N.D.Ill.1982). An additional wrinkle in the *New Mexico Natural Gas* case, however, was that the direct purchasers were in cahoots with the defendants; this was an independent ground for allowing the indirect purchasers to sue.

It is possible to allow indirect purchasers to sue in a case such as the present one without embracing the ill-defined "functional equivalent" approach of *In re Beef Industry Antitrust Litigation*, 600 F.2d 1148 (5th Cir. 1979); see also, e.g., *Gulf Oil Corp. v. Dyke*, 734 F.2d 797, 809 (T.E.C.A. 1984). That approach—effectively criticized in *In re Midwest Milk Monopolization Litigation*, 529 F.Supp. 1326, 1337-38 (W.D.Mo.1982), aff'd, 730 F.2d 528 (8th Cir.1984); Comment, *A Legal and Economic Analysis of the Cost-Plus Contract Exception in Hanover Shoe and Illinois Brick*, 47 U.Chi.L.Rev. 743, 756-70 (1980), cf. *Abbotts Dairies Division of Fairmont Foods v. Butz*, 584 F.2d 12, 16-17 (3d Cir.1978), and found to be inapplicable to conditions in the beef industry itself in *In re Beef Industry Antitrust Litigation*, 710 F.2d 216, 219-20 (5th Cir.1983)—requires elaborate analysis of the incidence of a cost increase, which is precisely the analysis that the Court disparaged in *Illinois Brick*. Our approach does not require this. We have formal cost-plus pricing in this case rather than its "functional equivalent." We

have formal cost-plus pricing, and more: a contract that required 100 percent passing on, and an acknowledgment of 100 percent passing on in every kilowatt hour resold to CILCO's residential consumers.

To determine whether (or to what extent) this case is within the rule of *Illinois Brick*, we must consider the reasons for confining the right to sue to the direct purchaser; for it is the reasons behind a rule that determine its scope. First, because the direct purchaser is closer to the violation and hence more likely to discover it, we want to make sure that he has a strong incentive to bring the violator to book, and we do this by holding out to him the prospect of recovering the entire damages caused by the violation if he wins the suit. Second, it is difficult to apportion damages between direct and indirect purchasers by the methods of litigation. A direct purchaser who finds himself paying a higher price for inputs would love to pass on all of the additional cost to his customers in the form of a higher price, but he cannot do so, because a price that much higher will so reduce the demand for his product that his profits will fall unacceptably. (If the higher price were optimal, the firm would have raised its price without waiting for its costs to increase.) The optimal adjustment by an unregulated firm to the increased cost of the input will always be a price increase smaller than the increase in input cost, and this means that the increased cost will be divided between the two tiers, the direct and indirect purchasers—but in what proportions will often be hard to determine, even by sophisticated techniques of economic analysis. This is a central insight of the *Illinois Brick* decision. An additional complication that further demonstrates the wisdom of the decision is that the higher input price may induce the direct purchaser to use more of an alternative input, and

this substitution will affect the proportion of the initial overcharge that the direct purchaser can recoup.

Where the direct purchaser has a cost-plus contract with his customers that requires them to buy a fixed quantity, the reasons for confining the right to seek damages to the direct purchaser cease to be fully persuasive. There is no longer a problem of apportionment, because the whole of any price increase will have been passed on to the customers by virtue of the contract. Yet the second reason for confining the right to seek damages to the direct purchaser survives: he has better information about the violation. And despite the cost-plus nature of the contract, he has everything to gain from suing. He will not have to share any of the damages that he recovers with his customers unless the contract contains a clause (or a court is persuaded to adopt an imaginative conception of unjust enrichment) that entitles them to any rebate he might receive, probably years later, on an input used in performing his side of the bargain. Nevertheless the Supreme Court has said that the indirect purchaser may sue if he has a cost-plus contract with the direct purchaser.

In the present case, where cost-plus pricing is imposed by public utility regulation rather than by a purely private, purely voluntary contract, the reasons balance out slightly differently, but the case for applying the cost-plus exception of *Illinois Brick* is no weaker once the balance is restruck. The public utility has less to gain from suit than the direct purchaser in the case of the purely private contract. The public utility commission may force the utility to pass on to the consumers any and all damages that the utility recovers, and if it does utilities will have no incentive to sue because they will have nothing to

gain from suit. In the present case CILCO finally did sue—but not until 1987, by which time the present suit was far advanced and the statute of limitations with regard to the damages incurred by residential customers in the present suit either had run or was about to run; and the CILCO case has remained dormant pending our decision of the appeal. CILCO seems a most reluctant suitor, and why shouldn't it be? It has little or nothing to gain by such a suit. Indeed, one might argue that public utility regulation (to the extent effective—admittedly a potentially big if) so far identifies a public utility with its customers as to bring the case within the separate exception recognized in *Illinois Brick* for situations in which the direct and indirect purchaser are under common control. See 431 U.S. at 736 n. 16, 97 S.Ct. at 2070 n. 16.

Although the amount of gas purchased by a utility's customers is not fixed in their contract with the utility (it would be absurd for consumers to commit to a fixed quantity; their need for gas varies with the weather!), the special character of a public utility eliminates the problem of apportionment, here with respect to the only class of customers that we believe should be allowed to sue, the residential customers. The retail distribution of natural gas through a grid of pipes to the customers' homes or places of business is a natural monopoly, *Omega Satellite Products Co. v. City of Indianapolis*, 694 F.2d 119, 123, 126 (7th Cir.1982); so, in the absence of regulation, a gas utility would charge a monopoly price. Although the efficacy of public utility rate regulation has been questioned (see, e.g., Stigler & Friedland, *What Can Regulators Regulate? The Case of Electricity*, 5 J.Law & Econ. 1 (1962); Moore, *The Effectiveness of Regulation of Electric Utility Rates*, 36 So.Econ.J. 365 (1970)), the facts

of this case suggest, and the parties seem to agree, that residential natural-gas rates in Illinois are lower because of regulation than they would be in an unregulated market, implying that CILCO has unused monopoly power in that market, which it exploited by passing on the full overcharge by Panhandle. The situation in the industrial market is different. Some industrial consumers of natural gas have good alternatives, and as to them CILCO apparently had no unused monopoly power that would have enabled it to shift the whole of the cost increase to them. Instead CILCO sought and obtained regulatory permission to reduce its profit margin on sales to these customers, thereby offsetting in part the higher rates enabled by the automatic pass-through provision.

CILCO's dealings with its industrial customers show why the absence of a quantity provision in a contract can make a difference. Since the industrial customers were not obligated to take a fixed (or their required) quantity of natural gas, and since they had competitive alternatives, CILCO's profit-maximizing course of action was to swallow part of the overcharge rather than try to pass it on dollar for dollar in the form of higher rates. But its residential consumers unlike its industrial customers had no good alternatives to natural gas (of which CILCO was the sole purveyor), at least in the short term, and CILCO's profit-maximizing course of action was therefore to allow its rates to them to rise by the exact amount that its gas costs rose as a result of Panhandle's alleged overcharge. It was not only the absence of competition but the presence of regulation that made this the profit-maximizing course of action; regulation is a stand-in for the quantity requirement in an ordinary contract. Apparently rate regulation had succeeded in keeping CILCO's rates to a level where an increase in those rates was bound to in-

crease the firm's revenues because the price increase (1) would not be offset by an equal or greater proportional decline in its sales and (2) would lead to a reduction in the firm's total costs (consumers would buy less, even if only a little less, at the higher price). CILCO therefore had every incentive to raise its price by the full amount allowed by the regulatory commission—which was the full amount of the gas overcharge. And it did it.

The significance of the regulatory setting is that if regulation keeps a utility's rates below what it would like to charge, the utility will raise those rates by the full amount allowed by the regulatory commission unless such an increase would carry the utility above its optimum rate. An unregulated firm would not do that, since as we have noted an unconstrained profit maximizer will always find it in its best interest to swallow a part of any cost increase that it experiences unless its customers are committed to a fixed quantity. It is unclear from the record in this court how generous the commission's allowance was; the commission may have allowed CILCO to double its rates—yet even so, if regulation forced CILCO to charge half or less of its preferred price, CILCO would pass on the entire cost increase. No one suggests that CILCO in fact absorbed any part of the increase, so far as sales to its residential customers were concerned.

The mechanics of the pass-through provision are pertinent. The "Uniform Purchase of Gas Adjustment Clause" that Illinois by statute requires CILCO to include in its contracts not only entitled but directed CILCO, if it paid Panhandle an extra penny per million cubic feet of gas, to add exactly one penny to each customer's bill for every Mcf of gas sold to that customer. So if all of its customers had continued buying the same amount of gas CILCO would have suffered no loss on account of

the overcharge. To the extent that CILCO lost residential sales because it was charging a higher price—and no doubt it lost some sales—the loss was not passed on to CILCO's customers (at least in any sufficiently direct way to escape the rule of *Illinois Brick*) and hence is not a component of the customers' damages. But by the same token this is not a case where successive links in the chain of distribution are claiming damages in respect of the same transaction. There are, instead, two completely different sets of transactions. One consists of sales to CILCO followed by resale to its residential customers; on these sales the entire overcharge came to rest on the residential customers and they alone suffered damage and can (on the view we take of the case) recover damages. The other set of transactions consists of the sales that CILCO lost because some customers balked at the higher rates; on these sales (or rather nonsales) the only loser is CILCO, and only CILCO can sue. There is no suggestion that the residential customers are suing or could sue to recover incidental expenses incurred by reducing their purchases of natural gas—the cost of an extra sweater or a more efficient furnace or better insulation.

To illustrate the distinction between the two types of loss in this case, suppose that the price to CILCO's residential customers before the (alleged) overcharge by Panhandle was $1 per Mcf, the overcharge was 10¢ per Mcf, and by operation of the Uniform Purchase of Gas Adjustment Clause the retail price rose to $1.10 because CILCO made no offsetting reduction in another component of the price, as it did with its industrial customers. And suppose that at the new, higher price CILCO sold only 950,000 Mcf, while at the old price it had sold 1,000,000 Mcf, and that nothing plausibly accounts for the decrease in sales except the price increase, which induced consumers to use less gas. Cf. *Illinois Power Co. v. Commissioner*, 792 F.2d 683, 687-88 (7th Cir.1986). The loss to each consumer would be the number of Mcf he bought at the new price times 10¢; the loss to CILCO would be its lost profits on the sales it did not make.

Thus there can be no problem of apportionment in the suit on behalf of the residential customers. Those customers are not seeking damages for gas they did not buy, and the damages for the gas they did buy can simply be read off from their gas bills. (Well, almost: at the beginning of each year the utility estimates the amount of rate increase necessary to cover any increase in its gas bill, and there is an adjustment at the end of the year based on actual experience.) Since CILCO can sue for its lost sales (this may be a component of its belatedly filed suit against Panhandle, although that is unclear from the complaint), there can be more than one set of plaintiffs. But each set will be suing in respect of different sales—not, as in *Illinois Brick*, the same sales.

We have said that proof of the indirect purchasers' loss would be straightforward. Proof of CILCO's lost sales would also be straightforward—at least as straightforward as is possible in an antitrust case. It would be a matter of comparing the utility's sales before and after the increase in gas prices, after correcting for other factors besides the increase that might have affected those sales. Such correction is not always easy, but it is a conventional aspect of calculating damages in antitrust cases; it has to be done in every case where the plaintiff claims to have lost sales because of the defendant's unlawful conduct and the defendant argues that the loss was due partly or entirely to other factors. See, e.g., *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 264, 66 S.Ct. 574, 579, 90 L.Ed. 652 (1946); *Fishman v. Estate of Wirtz*, 807 F.2d 520, 551

(7th Cir.1986); *id.* at 578 (partial dissent); *Olympia Equipment Leasing Co. v. Western Union Telegraph Co.*, 797 F.2d 370, 382-83 (7th Cir.1986). More important, it is a problem unrelated to the problem the Supreme Court wrestled with in *Hanover* and *Illinois Brick*. The Court was concerned with the situation where two purchasers of the same thing—the initial purchaser and the purchaser from the initial purchaser—are or could be complaining that both had been hurt, and the problem is to apportion the loss between them. Here only the residential consumers can complain about a loss from the overcharge on the gas they bought, while only CILCO can complain about a loss caused by the overcharge on gas that the residential consumers did not buy.

All this is not to say that *Illinois Brick* has no application to cases where the direct purchaser is subject to rate regulation. Although cost-plus is the spirit of rate regulation, the flesh is weak and often therefore the utility has considerable flexibility in pricing, much like an unregulated firm. Indeed, to the extent that it operates free from effective rate regulation—either because it faces competition which constrains its rates below the regulated level (apparently CILCO's situation with its industrial customers), or because the regulators are unable to prevent it from charging monopoly prices to its captive customers—the utility's situation is identical to that of an unregulated firm. But, if so, this will be revealed in the utility's decision to swallow some of the cost increase, as CILCO did with its industrial customers. In the case of its residential customers, regulation must have succeeded in forcing the utility to operate in a region of its demand curve where 100 percent passing on of any cost increase was the optimal strategy for the utility to follow, for that was the strategy it did follow.

With the rapid and unanticipated increases in fuel prices during the 1970s, utilities pressed for and obtained the right to include automatic fuel pass-through provisions in their contracts with customers, provisions that would allow the utility to pass on every dollar in higher prices that it paid for gas or other fuels to its customers without going through the time-consuming process of obtaining regulatory authorization to raise rates. Such provisions are also found in unregulated contracts, and should be treated the same there when the contract requires the buyer to take either a fixed quantity or his requirements, since a buyer cannot reduce his purchases under a requirements contract merely because he is dissatisfied with the terms of the contract as they have worked themselves out. See *Empire Gas Corp. v. American Bakeries Co.*, 840 F.2d 1333, 1340-41 (7th Cir.1988); *Wilsonville Concrete Products v. Todd Building Co.*, 281 Ore. 345, 352, 574 P.2d 1112, 1115 (1978); *Royal Paper Box Co. v. E.R. Apt Shoe Co.*, 290 Mass. 207, 195 N.E. 96 (1935); *Fort Wayne Corrugated Paper Co. v. Anchor Hocking Glass Corp.*, 130 F.2d 471, 473-74 (3d Cir.1942); White & Summers, Handbook of the Law Under the Uniform Commercial Code 126 (2d ed. 1980). (This example shows, by the way, why a rigid test of fixed quantity would be a senseless limitation on the cost-plus exception of *Hanover Shoe* and *Illinois Brick*—a buyer under a requirements contract does not have discretion as to the amount to take under the contract.) If on the other hand the buyer has complete flexibility as to how much to buy, a cost-plus provision is ineffectual; the buyer can always condition an agreement to buy a specific amount on the seller's agreeing to modify the contract by reducing the price. This is another reason for supposing that an agreement to take a fixed quantity, or, what is equivalent for these purposes, an

agreement to take one's requirements, is implicit in the cost-plus exception rather than an independent requirement for invoking it. The unexhausted monopoly power of a regulated utility takes the place of a fixed-quantity or requirements provision. The utility can force the whole of the cost increase through to its residential customers without sacrificing any profits, *and did so*.

[1, 2] But we do not think that the industrial customers should be allowed to sue for damages. By cutting its profit margin to them CILCO raised its price by less than the increase in gas cost, and while the division of that increase between the utility and its industrial customers is easy to ascertain—precisely because the utility was required to get approval for reducing its profit margin—we are unwilling to complicate the administration of *Illinois Brick* by trying to distinguish between difficult and easy apportionment cases. And the Supreme Court seemed unwilling to listen to such arguments. But for every cubic foot of gas bought by a residential customer, we *know* that the whole overcharge was passed on to the customers in accordance with the fuel pass-through provision of their contract with CILCO, and we know why (regulation plus the residential consumers' lack of alternatives).

It might seem an unimportant detail whether a buyer reacts to an overcharge by raising its price by less than the overcharge (as CILCO did with its industrial customers), thus losing fewer customers, or by raising its price by the full overcharge and thereby losing more customers than it would if it swallowed part of the overcharge. But in the second case the problem of apportioning losses on the same sales does not arise. It might also seem impermissible under *Illinois Brick* to inquire into

the question whether there really was 100 percent passing on; but the Court announced an exception for cases where there is a cost-plus contract, and there is such a contract here—the automatic fuel pass-through provision. Although it is not a contract for a fixed quantity or (what is equivalent for purposes of the exception) the buyer's requirements, the existence of public utility regulation is an adequate substitute in the circumstances.

True, we can never be absolutely certain that regulation has resulted in a 100 percent pass through; for all we know, CILCO would have sought a rate increase but for the gas overcharge, and by forbearing to do so in effect absorbed part of the overcharge. But by the same token, the seller under a fixed-quantity cost-plus contract might forbear to insist on a 100 percent pass through in order to curry favor with the buyer for the sake of future deals. No counterfactuals are certain, but the doubts here are too small to warrant our insisting that this potentially serious antitrust violation, which may have caused consumers of natural gas to pay almost $50 million in higher prices, shall go unremedied, as it may if we accept Panhandle's view of the scope of *Illinois Brick*. Whether the cost-plus exception might embrace other situations in which the direct purchaser has a cost-plus contract with the indirect purchasers but the contract does not require the indirect purchasers to buy a fixed quantity (or their requirements) is not a question that we need decide in this case.

The suit on behalf of the residential customers is within the scope of the cost-plus exception to the rule of *Illinois Brick* as we understand it, and we therefore affirm the denial by the district court of the defendant's motion to dismiss the complaint insofar as the complaint seeks

damages on behalf of CILCO's residential customers. We reverse insofar as the court allowed suit on behalf of the industrial customers for damages. We express no view of the antitrust merits or of the propriety of the requests for injunctive relief, and we award no costs in this court.

Affirmed in Part and Reversed in Part.

CUDAHY, Circuit Judge, concurring:

I concur without reservation in the majority's application of the *Illinois Brick* doctrine to the facts of this case. A bar to indirect purchaser suits would make very little sense if it were extended to the regulated natural gas distribution business where full purchased gas cost pass-through is incorporated in the retail rates The PGA clause transforms the transaction into the very epitome of a cost-plus contract. Likewise, because residential gas demand is inelastic in the short run due to the unavailability to residential customers of substitute fuels, a rough approximation of a fixed quantity term is present, whether or not required by *Illinois Brick*.

The Natural Gas Pipeline Association of America, in an amicus brief, argues that if the antitrust suit were left to the direct purchaser (CILCO), its regulator (the Illinois Commerce Commission) could and would direct CILCO to pass on the sums recovered to its customers. The customers would, therefore, be in as good a position as if the Attorney General had sued directly on their behalf. I believe this is essentially correct. CILCO has in fact now brought suit in this matter, presumably because the panel decision cast doubt on whether the Attorney General could maintain the action on behalf of consumers.

Under the practical facts of regulation CILCO would ordinarily have a greater incentive to bring this litigation

than economic theory suggests. An informal suggestion from its regulators that suit was appropriate to protect customers would ordinarily send CILCO to court. Further, regulation allows CILCO to recognize only its *prudently incurred* expenses for ratemaking purposes. Presumably, a distribution company's purchase of pipeline gas at prices inflated by antitrust violations could be challenged as an imprudent incurrence of operating expenses. An antitrust recovery would at least partially offset any imprudence in the initial purchasing decision. In any event, in its next rate case, the distribution company would be hard pressed to justify its payment of illegally inflated prices if neither it nor the Attorney General had sought to press the antitrust claim.

Nonetheless, I suspect that considerations such as the difficulty of settlement might lead CILCO to prefer an Attorney General's lawsuit to its own. Presumably, a settlement by the state Attorney General with the pipeline supplier would be accepted as fully arm's length and justifiable. Were CILCO to settle, however, the aggressiveness of its stance might be questioned by the regulators in light of its ongoing relationship with the supplier and, of course, its settlement would in all probability have to be approved by the regulatory authority. It therefore seems to me that, in the final balance, suit by CILCO is not necessarily preferable to suit by the Attorney General on behalf of the residential customers.

FAIRCHILD, Senior Circuit Judge, with whom BAUER, Chief Judge, and CUMMINGS and MANION, Circuit Judges, join, concurring in part, dissenting in part.

I concur in reversal as to the treble damage claims on behalf of industrial customers. I respectfully dissent from affirmance with respect to such claims on behalf of residential customers.

The residential customers purchase from CILCO, and are only indirect purchasers from Panhandle, who allegedly overcharged CILCO. Because the rates charged by CILCO reflect, approximately at least,[1] the actual cost of gas, it is claimed that the residential customers were "injured" so as to be entitled to treble damages under § 4 of the Clayton Act, 15 U.S.C. § 15,[2] by reason of the pass-on of the overcharge.

The Supreme Court has "held that, except in certain limited circumstances, a direct purchaser suing for treble damages under § 4 of the Clayton Act is injured within the meaning of § 4 by the full amount of the overcharge paid by it . . .". *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 724, 97 S.Ct. 2061, 2064, 52 L.Ed.2d 707 (1977) (footnote omitted) (interpreting the rationale of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 494, 88 S.Ct. 2224, 2232, 20 L.Ed.2d 1231 (1968)). *Hanover Shoe* had rejected an attempt by an antitrust defendant to establish that plaintiff direct buyer had not been "injured" within the meaning of § 4 because the direct buyer had passed on any overcharge. In *Illinois Brick*, plaintiff was asserting a claim on behalf of indirect purchasers that they had been "injured" by a pass-on of an overcharge. The Court reaffirmed *Hanover Shoe* and decided that its root principle (that, with limited exceptions, the full injury of the overcharge falls upon the direct purchaser) must apply to and prevent treble damage claims on behalf

1. The process of adjustment of rates charged by CILCO to rates paid is described in the panel opinion. 839 F.2d at 1208 n. 2.

2. Section 4 provides that

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor . . . and shall recover threefold the damages by him sustained. . . .

of an indirect purchaser, as well as apply to and permit claims of a direct purchaser.

Both *Hanover Shoe* and *Illinois Brick* dealt with the question presented as one of statutory construction of § 4. Indeed in *Illinois Brick*, the Court said,

> In considering whether to cut back or abandon the *Hanover Shoe* rule, we must bear in mind that considerations of *stare decisis* weigh heavily in the area of statutory construction, where Congress is free to change this Court's interpretation of its legislation.

431 U.S. at 736, 97 S.Ct. at 2070.

Illinois Brick described only two exceptions to its general rule that the direct purchaser is injured by the full amount of the overcharge. One, "where the direct purchaser is owned or controlled by its customer," 431 U.S. at 736, n. 16, 97 S.Ct. at 2070, n. 16, is clearly inapplicable here. The other, which originated in *Hanover Shoe*, is where an overcharged direct buyer has a preexisting cost-plus contract for a fixed quantity. 431 U.S. at 736, 97 S.Ct. at 2069.

Judge Posner's opinion for this court suggests that the reference to "a fixed quantity" does not have controlling significance. *Ante*, pp. 893 and 894. Particular aspects of the *Hanover Shoe* and *Illinois Brick* opinions persuade me otherwise.

The *Hanover Shoe* opinion, in recognizing that "a preexisting 'cost-plus' contract" might provide an exception to its rule against a pass-on defense, did not expressly require a fixed quantity element. 392 U.S. at 494, 88 S.Ct. at 2232. That element may well have been implied, for the Court referred to the cost-plus contract as "thus mak-

ing it easy to prove that [the direct buyer] has not been damaged." *Ibid.* In *Illinois Brick,* Justice White, who wrote for the Court in both cases, expressly referred to the fixed quantity element and took pains to explain why it was important:

> But this Court in *Hanover Shoe* indicated the narrow scope it intended for any exception to its rule barring pass-on defenses by citing, as the only example of a situation where the defense might be permitted, a pre-existing cost-plus contract. In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price. The effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand that complicates the determination in the general case.

431 U.S. at 735-36, 97 S.Ct. at 2069-70.

This court's opinion concedes that no doubt CILCO lost residential sales because of the higher price, and because of the overcharge if there was one. *Ante,* p. 896. It follows from *Hanover Shoe* and *Illinois Brick* that when some injury falls on the direct purchaser because of the overcharge, it all does.

After considering and rejecting proposed exceptions, the Court said "As we have noted, *supra* at 735-36, [97 S.Ct. at 2069-2070], *Hanover Shoe* itself implicitly discouraged the creation of exceptions to its rule barring pass-on defenses, and we adhere to the narrow scope of exemption indicated by our decision there." 431 U.S. at 745, 97 S.Ct. at 2074.

As I read *Illinois Brick,* the Supreme Court did not leave it to the discretion of the lower courts to create new exceptions for situations which fall within some range of approximation of the exceptions defined by the Court. And that is what this court appears to be doing with respect to the claims of the residential customers.

(2)

No. 88-2109

In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI,
As Parens Patriae,

Petitioners,

vs.

THE KANSAS POWER AND LIGHT COMPANY
and UTILICORP UNITED INC.,

Respondents.

On Petition For A Writ Of Certiorari To The
United States Court Of Appeals For The Tenth Circuit

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QUESTION PRESENTED

Petitioners' statement of "Questions Presented" violates Supreme Court Rule 21.1(a) by presenting argumentative and repetitious questions. The question certified by the District Court for interlocutory appellate review, decided by the United States Court of Appeals for the Tenth Circuit pursuant to 28 U.S.C. § 1292(b), and presented to this Court asks:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

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No. 88-2109

In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI,
As Parens Patriae,

Petitioners,

vs.

THE KANSAS POWER AND LIGHT COMPANY
and UTILICORP UNITED INC.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

RESPONDENTS' BRIEF IN OPPOSITION

Respondents The Kansas Power and Light Company[1] and UtiliCorp United Inc.[2] respectfully request that this

[1] In compliance with Supreme Court Rule 28.1, The Kansas Power and Light Company states that it has two wholly-owned subsidiaries, Rangeline Corporation and Gas Service Energy Corporation, and that it acquired the former Gas Service Company in 1983.

[2] In compliance with Supreme Court Rule 28.1, UtiliCorp United Inc. states that it is a publicly-held electric and natural gas utility operating in seven states through five divisions and in one Canadian province through a wholly-owned subsidiary. In addition to these utility operations, UtiliCorp has three other wholly-owned subsidiaries.

Court deny the petition for writ of certiorari, seeking review of the opinion of the United States Court of Appeals for the Tenth Circuit in this case.

STATEMENT OF THE CASE

A. Background

The Kansas Power and Light Company ("KPL") is both an industrial natural gas consumer and a natural gas distribution company which serves residential, commercial, and industrial customers in the states of Kansas, Missouri, Oklahoma, and Nebraska. UtiliCorp United Inc. ("UtiliCorp") provides natural gas to industrial, commercial, and residential customers in western Missouri and Lawrence, Kansas, through its Missouri Public Service and Kansas Public Service divisions.

KPL and UtiliCorp (also referred to herein as "the utilities") purchased natural gas directly from Williams Natural Gas Company ("Pipeline"). Pipeline had purchased that gas from Amoco Production Company ("Amoco"), Cities Service Oil & Gas Corporation ("Cities Service"), CSG Exploration Company ("Exploration"), the Moxa Limited Partnership ("Moxa"), and the Wamsutter Limited Partnership ("Wamsutter").

In September of 1984, KPL filed a complaint pursuant to Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982), against defendants Pipeline, Amoco, Cities Service, Exploration, Moxa, and Wamsutter. KPL alleges, *inter alia*, that the defendants, acting in combination, artificially

inflated and fixed the price of natural gas that was produced by them in Wyoming and sold in interstate commerce by Pipeline to KPL, UtiliCorp, and other direct natural gas purchasers. UtiliCorp subsequently intervened and filed a substantially similar complaint against the same defendants.

KPL and UtiliCorp seek to recover overcharge damages for all natural gas purchased directly from the defendants which was used by the utilities in their own operations or was resold to their residential, industrial, and commercial customers. KPL and UtiliCorp also seek to recover resale profits lost as a result of defendants' anticompetitive conduct. The defendants claimed as an affirmative defense that the utilities passed on any illegal overcharges to their customers and therefore lacked standing under Section 4 of the Clayton Act.

Following KPL's lead, the states of Kansas and Missouri ("the States") filed complaints under Section 4 of the Clayton Act against the same defendants in July of 1985 and August of 1986, respectively. The States' complaints are nearly identical to KPL's complaint and the subsequent complaint of UtiliCorp. The States seek to recover overcharge damages on behalf of state agencies and municipalities[3] that purchased gas directly or

[3] The States' claims on behalf of cities which distribute natural gas to their residents through a municipal utility are entirely analogous to the claims of KPL and UtiliCorp. For example, the City of Springfield, Missouri, is a named plaintiff with claims on behalf of all its customers, including industrial and commercial purchasers.

indirectly from Pipeline and as *parens patriae* on behalf of indirect residential gas customers in their respective states.

The States do not – and indeed cannot – assert claims on behalf of the utilities' industrial and commercial gas customers in Kansas and Missouri, or on behalf of KPL's residential, industrial, and commercial gas customers in Nebraska and Oklahoma. As a result, the States' *parens patriae* claims represent no more than 50% of the natural gas sold by the defendants in Missouri and Kansas. Recognition of the States' *parens patriae* claims, and the defendants' corresponding pass-on defenses, would therefore eliminate more than 50% of the antitrust damages asserted by the utilities in this case against the defendant producers and suppliers.

B. Proceedings Below

KPL and UtiliCorp filed motions to strike or for partial summary judgment on those affirmative defenses that were based on the pass-on theory rejected in *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968). The District Court found on uncontested evidence that neither KPL nor UtiliCorp resold natural gas pursuant to cost-plus contracts for fixed quantities. *In re Wyoming Tight Sands Antitrust Cases*, 695 F. Supp. 1104 (D. Kan. 1988), *aff'd*, 866 F.2d 1286 (10th Cir. 1989); Appendix to States' Petition for Writ of Certiorari at 34 ("A34"). Accordingly, it entered partial summary judgment prohibiting defendants from asserting pass-on defenses to the utilities' antitrust claims. A37.

The District Court also dismissed *sua sponte* the States' *parens patriae* claims pursuant to the holding of *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), prohibiting offensive use of pass-on theories. In so ruling, the District Court made no determination regarding the amount of illegal overcharges allegedly passed on by KPL or UtiliCorp to their customers. A34.

None of the defendants appealed from the District Court's entry of partial summary judgment prohibiting use of pass-on defenses. The States were granted an interlocutory appeal solely to determine whether residential indirect purchasers of natural gas may join their own local distribution companies in asserting federal antitrust claims against the producers and an intermediary pipeline supplier of natural gas.

The Tenth Circuit properly concluded that the rulings and rationales underlying *Hanover Shoe* and *Illinois Brick* prohibit the needless and expensive complication of ongoing federal antitrust litigation which the States' *parens patriae* claims would cause. *In re Wyoming Tight Sands Antitrust Cases*, 866 F.2d 1286, 1292 (10th Cir. 1989); A12. Affirming the District Court's Order, the Court below distinguished the decision of the Court of Appeals for the Seventh Circuit in *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S. Ct. 543, 102 L. Ed. 2d 573 (1988) ("*Panhandle Eastern*"). A13-14.

The Tenth Circuit observed that *Panhandle Eastern* was based on numerous facts neither established nor

present in this case.[4] A13. In particular, the Tenth Circuit stressed that the Seventh Circuit in Panhandle Eastern was faced with the residential consumers of a single utility, while the plaintiffs in this case include "utilities that occupy different levels on the distribution chain within two states, and . . . two states and their attendant public utility rate regulation schemes."[5] A13.

The States' petition raises the question of whether KPL and UtiliCorp, as direct purchasers from an anticompetitive combination, should be permitted to proceed under Section 4 of the Clayton Act on behalf of themselves and for the benefit of their industrial, commercial, and residential customers without further delay, additional expense, and unnecessary complication. That question can and should be resolved by denying the States' petition.

REASONS FOR DENYING THE WRIT

The States' petition should be denied for three reasons:

First, the Tenth Circuit's decision in this case faithfully follows the Court's rulings in *Hanover Shoe* and *Illinois Brick*. The States' petition is thus a direct challenge to the sensible *Illinois Brick* rule. This Court should decline the States' invitation to reinstate the process of individual market classification rejected in *Illinois Brick*.

Second, this Court in *California v. ARC America Corp.*, 490 U.S. ___, 109 S. Ct. 1661, 104 L. Ed. 2d 86 (1989)("*ARC America*"), reaffirmed the direct purchaser rule of *Illinois Brick* for federal antitrust claims, but expressly permitted state attorneys general to assert claims on behalf of indirect residential purchasers pursuant to state antitrust law. No need exists to reexamine the *Illinois Brick* rule.

Third, significant factual differences explain conclusions reached by the Tenth Circuit in this case and the Seventh Circuit in *Panhandle Eastern*. Certiorari should be denied because no fundamental conflict currently exists between those Circuits regarding the policies and purposes underlying *Hanover Shoe* and *Illinois Brick*.

I. Certiorari Should Be Denied Because The Tenth Circuit's Decision Is Totally Consistent With This Court's Rulings In *Hanover Shoe* And *Illinois Brick*.

In *Illinois Brick*, this Court recognized that "the process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid." *Illinois Brick*, 431 U.S. at 744-45. The Court further noted that "*Hanover Shoe* itself implicitly discouraged the creation of exceptions to its rule barring pass-on defenses" and adhered to the narrow scope of exemption indicated in that decision. *Id.* at 745.

[4] The Seventh Circuit itself had conceded earlier that the District Court's findings in *Wyoming Tight Sands* were distinguishable. A14, *citing Panhandle Eastern*, 852 F.2d at 893.

[5] Moreover, as a "one city" utility until 1986, UtiliCorp's Kansas Public Service operation was not subject to the authority of the Kansas Corporation Commission until 1987 and did not resell natural gas by way of a Purchased Gas Adjustment mechanism until that time.

Because the Court of Appeals closely followed the rulings and rationales of *Hanover Shoe* and *Illinois Brick*, the States unfairly brand the Tenth Circuit's opinion as mechanical. Petition at 7. On the contrary, the Court below applied *Hanover Shoe* and *Illinois Brick* carefully and correctly to avoid the addition of unnecessary complexity and expense to this case and to ensure the efficient enforcement of federal antitrust law in the future. *See* A9-13.

In particular, the Tenth Circuit noted that "[c]omplex issues of proof will grow geometrically if the States press their consumers' demands," due in part to the unresolved factual issue of how much illegal overcharge was passed on to the residential consumers of each utility. A10. Contrary to the States' promise of simple damage apportionment, the Court below recognized that "[a]ny allocation of illegal overcharges to the residential consumers may require tracing the sale from the wellhead through each level of distribution in order to establish the amount of illegal gas costs actually paid by the consumers in each state. . . ." A12. The Tenth Circuit also correctly observed that even a perfect pass-on of all overcharges would not eliminate the need to apportion the damages sustained by KPL and UtiliCorp as a result of decreased demand caused by defendants' inflated prices. A12-13.

Finally, the Court of Appeals noted that permitting the States to pursue their claims in this case would imperil vigorous enforcement of the antitrust laws in the future. A10, 11. Such action would shift the incentive to prosecute alleged antitrust violators away from the direct purchaser, who is closer to the violator and presumably has better knowledge, and transfer the cost of policing and enforcing the antitrust

laws to the states. A10, 14. The Tenth Circuit recognized that the States' incentive to join in this particular action provides no assurance whatsoever of aggressive antitrust enforcement in other cases.[6] A10, 11.

The States fail to address these critical issues in their petition. Instead, they seek certiorari by assuming a perfect pass-on of all overcharges and claiming that such damages are "readily-identifiable" and "easily-proven." Such assumptions neither require nor justify a reexamination of *Hanover Shoe* and *Illinois Brick*. The States' petition prays for nothing more than a prohibited individual market classification and therefore should be denied.

II. Certiorari Should Be Denied Because This Court Fully Defined The Cost-Plus Exception to the Direct Purchaser Rule In *Illinois Brick* and Permitted a State Law Remedy For Indirect Purchasers in *ARC America*.

The States contend that certiorari is necessary because the Court never has "addressed or explained" the "precise nature and scope" of the cost-plus exception to the *Illinois Brick* direct purchaser rule. Petition at 10-11. The States' contention is incorrect.[7]

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[6] This Court is well aware of the extraordinary expenses required to prepare competently a complicated antitrust case. KPL – as the direct purchaser of 80 percent of the gas at issue in this case – has taken the lead and paid the vast majority of expenses. The States' desire to join and remain in this action with KPL and UtiliCorp is directly related to their ability to share expenses with the utilities. Far less certain is the States' incentive or ability to bring an action independently in the future if the *Illinois Brick* rule is changed.

[7] The *Illinois Brick* rule and its narrow exceptions are well understood and routinely enforced by the lower courts. The

(Continued on following page)

The Court originally indicated that the cost-plus contract exception might be applicable when the direct purchaser "has not been damaged." *Hanover Shoe*, 392 U.S. at 494. The Court specifically recognized, however, that direct purchasers would incur recoverable damages if total sales declined as a result of illegal overcharges. *Id.* at 493.

In *Illinois Brick*, the Court explained that the cost-plus contract exception to the rule barring offensive and defensive use of pass-on theories applies only if "the purchaser is insulated from any decrease in its sales as a

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five cases cited by the States in their petition at 11 n.9 do not establish that lower courts are confused and in conflict regarding proper application of the *Illinois Brick* rule. Three of the cited cases properly rejected a regulated rate exception. *See U.S. Oil Co. v. Koch Refining Co.*, 518 F. Supp. 957, 962-63 (E.D. Wis. 1981); *Go-Tane Service Stations, Inc. v. Ashland Oil, Inc.*, 508 F. Supp. 200 (N.D. Ill. 1981); *City of Cleveland v. Cleveland Elec. Illuminating Co.*, 538 F. Supp. 1320, 1323-24 (N.D. Ohio 1980).

The residential customers in the fourth case, like KPL and UtiliCorp in this case, constituted the first direct purchasers from the conspiring defendants. *See In re New Mexico Natural Gas Antitrust Litigation*, 1982-1 Trade Cases (CCH) ¶ 64, 685 (D.N.M. 1982). The holding in that case, therefore, is consistent with the direct purchaser rule. The final case cited, *In re Beef Industry Antitrust Litigation*, 600 F.2d 1148 (5th Cir.), *cert. denied*, 449 U.S. 905 (1980), is also inapplicable because the "functional equivalent" test set forth therein requires "precisely the analysis that the Court disparaged in *Illinois Brick*." *Panhandle Eastern*, 852 F.2d at 894. *See also County of Oakland v. City of Detroit*, 866 F.2d 839 (6th Cir. 1989) (counties are proper parties to assert antitrust claims despite pass-on of excessive costs).

result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." *Illinois Brick*, 431 U.S. at 736. Certiorari should be denied precisely because such facts are not present in this case.

In *ARC America*, this Court recently reaffirmed the direct purchaser rule, stating flatly that "[a]s construed in *Illinois Brick*, § 4 of the Clayton Act authorizes only direct purchasers to recover monopoly overcharges under federal law." 109 S. Ct. at 1666; 104 L. Ed. 2d at 96. Nevertheless, the Court also held that state attorneys general are free to pursue claims on behalf of indirect residential purchasers by initiating *parens patriae* actions under state antitrust law. *Id.* No need now exists to multiply the complexity and expense of this action simply to revisit a rule reaffirmed in April of this year. Accordingly, the States' petition for writ of certiorari should be denied.

III. Certiorari Should Be Denied Because No Fundamental Conflict Currently Exists Between The Tenth And Seventh Circuits Regarding The Policies And Purposes Underlying *Hanover Shoe* and *Illinois Brick.*

The Tenth Circuit specifically noted the following critical differences between the facts in this case and the facts underlying the Seventh Circuit's decision in *Panhandle Eastern*:

1. Unlike this action, which was initiated by KPL in 1984, the plaintiff utility in *Panhandle Eastern* had delayed filing suit, and a serious question existed as to whether the statute of limitations had expired on the utility's claim. A13;

2. The Court in *Panhandle Eastern* dealt with the customers of a single utility in a single state with a single set of rate regulations, while this action involves numerous utilities operating in at least two separate states with two rate regulation schemes. A13;

3. The Court in *Panhandle Eastern* was not required to sacrifice the overcharges passed on to the commercial and industrial customers of the utility, in stark contrast to the elimination of more than 50% of the damages claimed by the utilities that will occur in this case if the States' pass-on theories are permitted. A14;

4. No doubt existed in *Panhandle Eastern* that all overcharges were passed-on by the utility, and no need existed to apportion damages between the direct and indirect purchasers, while in this case the Tenth Circuit noted that "the amount of overcharge passed on may be an unresolved question of fact." A14.

Each of these facts was considered by the Seventh and Tenth Circuits in reaching their respective decisions.

Although the rulings in this case and in *Panhandle Eastern* differ, no conflict exists between the Tenth and Seventh Circuits regarding the policies and purposes underlying the *Hanover Shoe* and *Illinois Brick* rules. Both courts recognized the need to preserve incentives for effective and efficient enforcement of the federal antitrust laws. Under the facts of this case, the Tenth Circuit faithfully served those policies and accomplished that purpose by refusing to recognize a public utility exception to the direct purchaser rule of *Illinois Brick.* The Seventh Circuit in *Panhandle Eastern* felt compelled by the facts of that case to take different action to achieve the same end.

The Seventh Circuit candidly admitted in *Panhandle Eastern* that "we can never be absolutely certain that regulation has resulted in a 100 percent pass through. . . ." *Panhandle Eastern,* 852 F.2d at 898. The Seventh Circuit then explained that it ruled as it did because "the doubts here are too small to warrant our insisting that this potentially serious antitrust violation, which may have caused consumers of natural gas to pay almost $50 million in higher prices, shall go unremedied, as it may if we accept Panhandle's view of the scope of *Illinois Brick.*" *Id.* The Seventh Circuit's result-oriented decision, whether correct or incorrect, does not evidence a fundamental conflict with the Tenth Circuit sufficient to require or justify granting certiorari in this case.

CONCLUSION

For the reasons set forth above, the petition of the states of Kansas and Missouri as *parens patriae* for a writ of certiorari should be denied.

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(4)

No. 88-2109

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THE STATES OF KANSAS AND MISSOURI,
AS *PARENS PATRIAE*,
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REPLY BRIEF OF PETITIONERS

The petition for writ of certiorari filed by the States of Kansas and Missouri should be granted. The brief in opposition fails to distinguish Judge Posner's recent opinion for the *en banc* Seventh Circuit, which reached the opposite result from the Tenth Circuit below on identical facts.

Instead of acknowledging that the Court has never directly addressed the scope of any exception to the direct-purchaser rule of *Illinois Brick* and *Hanover Shoe*,[1] the respondent utility companies merely restate the general rule itself and discuss its rationale. But it is the confusion surrounding the cost-plus *exception* to the direct-purchaser rule that needs the Court's attention. The proper scope of that exception is squarely presented here.

1. *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977); *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968).

I. The Tenth Circuit's Refusal to Apply the Exception to the *Illinois Brick* Direct-Purchaser Rule Recently Recognized by the En Banc Seventh Circuit Creates a Direct Conflict on a Pure Question of Law.

This case presents a pure question of law: is there an exception to the general rule that only direct purchasers have standing to sue where there is a perfect and easily-provable pass-through of all illegal overcharges to residential utility consumers? In granting summary judgment below, the Tenth Circuit *assumed* a perfect pass-through and answered "no"; after considering the record in *Panhandle Eastern*,[2] the Seventh Circuit *found* these same facts, and answered "yes." The Court should grant certiorari to resolve this purely legal conflict.

Respondents' supposed "distinctions" between this case and *Panhandle Eastern* are neither meaningful nor relevant. The utilities first suggest that the claims of the direct-purchaser utility in *Panhandle Eastern* may have been time-barred. Whether the *direct* purchaser's claims happen to be barred should not affect the standing of *indirect* purchasers under the cost-plus exception. The present case in any event is no different from *Panhandle Eastern* in this respect because claims of UtiliCorp, one of the two plaintiff utilities below, may be time-barred as well.[3]

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2. *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Corp.*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S.Ct. 543 (1988).

3. Although UtiliCorp was a plaintiff in this case in 1985, it dismissed its Complaint in February, 1986, and did not seek to re-enter the litigation until it filed a motion to intervene in June, 1987.

Respondents' argument that the indirect purchasers in *Panhandle Eastern* were all residents of a single state also presents no meaningful distinction. Although the consumers here reside in two states, Kansas and Missouri, the regulatory mechanisms in those states operate identically to require 100% of the overcharges incurred by the utilities to be passed on to the residential consumers.[4] Because the end result to Missouri and Kansas residents is the same, the fact that they reside in different states cannot matter.

The suggestion that more than 50% of the respondent utilities' claims will be lost if the states are granted standing, while in *Panhandle Eastern* no overcharges were "sacrificed," is also without merit. Although *Panhandle Eastern* allowed the State of Illinois to recover all illegal overcharges incurred by residential customers, the overcharges incurred by the commercial and industrial customers (these customers do not fit within the exception to the direct-purchaser rule) were still recovered by the utilities, as were the utilities' own lost profits. App. E, A54-58. Application of *Panhandle Eastern's* reasoning yields the same result in the present case: no overcharges will be sacrificed.[5] Claims will be lost only if the petitioner states are *not* allowed to assert claims on behalf of their residents.[6]

---

4. *See* Petition for Writ of Certiorari at 4, n.3.

5. In its brief in the Tenth Circuit, UtiliCorp conceded that its "recovery of damages on behalf of its industrial customers is unaffected by the Seventh Circuit's opinion in *Panhandle Eastern*." *See* Brief for Plaintiff-Appellee UtiliCorp United, Inc. at 20-21.

6. Because at least one Kansas utility did not file suit to recover the overcharges it passed on, the claims of more than 50,000 Kansas residential consumers will be lost if the states

(Continued on following page)

Respondents' final argument—that the precise percentage of overcharges they passed through to consumers may be factually unresolved—also misses the mark. At no point do respondents deny what is in fact the case: they passed on *all* overcharges incurred. Moreover, the Tenth Circuit "assume[d] . . . for the purpose of deciding the issues before [it] that there was a perfect and provable pass-on of the allegedly illegal overcharge." *See* App. A, A14. Both the decision below and *Panhandle Eastern* thus involved a 100% pass-on of the illegal overcharges.

The decision below conflicts with *Panhandle Eastern* on an important question of antitrust law that the Court has never directly addressed. The petition should be granted.

II. Respondents' Reliance on California v. ARC America Is Misguided Because the Court There Did Not Address the Scope of the Cost-Plus Exception.

Respondents contend that the precise scope of the cost-plus exception has already been fully explained by the Court. But respondents cannot point to a single case where the Court has considered a concrete exception to the direct-purchaser rule. Neither *Hanover Shoe* nor *Illinois Brick* announced an actual exception to the rule; the Court instead merely suggested that under certain circumstances *not presented* in those cases an exception *may* exist.

Footnote continued—

are denied standing. *See* Petition for Writ of Certiorari at 4, n.2. If, as seems likely, respondent UtiliCorp's claims were not timely filed, the claims of the many Missouri residents who were customers of that utility also will go unredressed if the *parens patriae* claims are not allowed to proceed.

California v. ARC America[7] did not end the confusion. There the Court also did not directly consider the cost-plus exception,[8] but once again simply suggested that such an exception *might* exist on appropriate facts: "[W]e implicitly recognized [in *Illinois Brick*] . . . that indirect purchasers *might* be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them." 109 S.Ct. at 1666, n.6 (emphasis added).

It is this Court's discussion of hypothetical exceptions, rather than real ones, that led to the present conflict between the Seventh and Tenth Circuits. In holding that the residential consumers here lack standing despite the same perfect and provable pass-through of overcharges considered by the Seventh Circuit, the Tenth Circuit stated: "[T]he Supreme Court did not say this would constitute an exception but rather that it 'might be,' and for this reason we have narrowly construed the exception . . . ." App. A, A8.

The antitrust damages in the present case, involving a readily-identifiable, 100% pass-through of all overcharges, would be "easy to prove" within the meaning of *ARC America* and *Illinois Brick*. The state attorneys general, proceeding as *parens patriae* on behalf of their injured state residents, have ample incentive to sue; the utilities' own incentive is questionable in view of their complete pass-through of overcharges. This case thus presents the very facts the Court has repeatedly indicated "might" constitute an exception to the direct-purchaser rule. Certiorari should issue to clarify whether and to what extent such an exception actually exists.

7. *California v. ARC America*, 109 S.Ct. 1661 (1989).

8. The issue in *ARC America* was instead whether *Illinois Brick* and *Hanover Shoe* preempted state antitrust laws permitting indirect purchaser suits.

CONCLUSION

Whether the interests of residential consumers are better represented by the utilities that passed on all overcharges to them, or by state attorneys general acting in their *parens patriae* capacity, is a question of considerable importance to antitrust enforcement. The Court should issue a writ of certiorari to review the decision of the Tenth Circuit and to resolve the split of authority in the circuits that now exists.

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No. 88-2109

In the Supreme Court of the United States

OCTOBER TERM, 1989

THE STATES OF KANSAS AND MISSOURI,
AS *PARENS PATRIAE*,
Petitioners,

vs.

THE KANSAS POWER & LIGHT COMPANY

and

UTILICORP UNITED, INC.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

SUPPLEMENTAL BRIEF OF PETITIONERS

A RECENT DECISION IN THE SIXTH CIRCUIT FURTHER HIGHLIGHTS THE CONFLICT AND CONFUSION IN THE CIRCUITS OVER THE SCOPE OF THE ILLINOIS BRICK EXCEPTION TO THE DIRECT-PURCHASER RULE

Petitioners file this supplemental brief pursuant to Rule 22.6 to call the Court's attention to two developments:

1. The Sixth Circuit in *County of Oakland v. City of Detroit*, 866 F.2d 839 (6th Cir. 1989), has re-

cently construed the same question presented in this case—the scope of the *Illinois Brick*[1] cost-plus exception—in a manner that it apparently concedes is contrary to the Seventh Circuit's decision in *Panhandle Eastern*.[2] This new decision heightens the conflict among the circuits on the questions presented by the instant petition for certiorari.

2. Three petitions for certiorari have been filed in this Court seeking review of the Sixth Circuit's opinion in *County of Oakland*:

   (a) No. 89-56, *Allevato v. County of Oakland*, 58 U.S.L.W. 3025 (U.S. July 13, 1989).

   (b) No. 89-79, *City of Detroit v. County of Oakland*, 58 U.S.L.W. 3026 (U.S. July 14, 1989).

   (c) No. 89-101, *Young v. County of Oakland*, 58 U.S.L.W. 3078 (U.S. July 17, 1989).

The Sixth Circuit in *County of Oakland* addressed the exact *Illinois Brick* issue that led to the original split between the Seventh Circuit in *Panhandle Eastern* and the Tenth Circuit in the present case. *County of Oakland* reversed a district court decision that had allowed indirect purchasers of a regulated service to sue. Even though it assumed that 100% of the alleged overcharges were passed on to the ultimate consumers,[3] the

1. *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977).

2. *State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S.Ct. 543 (1988).

3. The court stated that the real issue before it was whether the direct-purchaser counties were precluded from suing "if one assumes—as we do, for purposes of this opinion—that any and all overcharges were passed on to the counties' own customers,

(Continued on following page)

Sixth Circuit decided to read the cost-plus exception in *Illinois Brick* narrowly:

> Mindful . . . "of the *Illinois Brick* Court's emphasis upon the narrow scope of exemptions to the indirect-purchaser rule," we are not persuaded that a cost-plus contract exception, assuming it exists, precludes the direct purchaser from maintaining suit in the case at bar.

866 F.2d at 849.

Although the Sixth Circuit's original opinion in *County of Oakland* did not refer to the decisions in either the present case or *Panhandle Eastern*, on rehearing the Sixth Circuit considered and expressly refused to follow *Panhandle Eastern*:

> Although at least one court has been prepared to read the cost-plus exception more broadly in cases involving offensive use of a pass-on theory, *see State of Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 [(7th Cir. 1988) (en banc), *cert. denied*, ... U.S. ...., 102 L. Ed. 2d 573 (1988), we do not think the purposes of the antitrust laws would be well served by reading the cost-plus contract exception so broadly in a case involving the defensive use of the pass-on theory.]

866 F.2d at 852.[4]

Footnote continued—

the municipalities." 866 F.2d at 845. This assumption of a 100% pass-through was identical to the one made by the Tenth Circuit in the present case.

4. The bracketed portion of this sentence was omitted from the published opinion due to a typographical error. The complete sentence can be found at 1989-1 Trade Cas. (CCH) ¶ 68,571, at 61,047, and at 30a of the Appendix to the Petition for Certiorari in No. 89-79, *City of Detroit v. County of Oakland*.

At least three different circuits are now split on the same issue of antitrust enforcement. Both the Sixth and Tenth Circuits have studied, and rejected, Judge Posner's opinion for the *en banc* Seventh Circuit, and appear to have decided in effect that there is no exception to the direct-purchaser rule, even where 100% of all alleged overcharges have been passed on in a regulated environment.[5] The full extent and importance of the conflict among the circuits is confirmed by the questions presented in the three certiorari petitions arising from the *County of Oakland* case, which precisely mirror the questions presented here.

The confusion in the lower courts is evident. The issue is an important one that is squarely presented by the present facts. Certiorari should be granted.

5. Still another circuit, the Fifth, has, contrary to the Sixth and Tenth Circuits' approach, found an exception to the direct-purchaser rule where the "functional equivalent" of a cost-plus contract exists, regardless of whether a "fixed quantity" is involved. *See In re Beef Indus. Antitrust Litig.*, 600 F.2d 1148, 1163-64 (5th Cir. 1979), *cert. denied*, 449 U.S. 905 (1980).

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No. 88-2109

In the Supreme Court of the United States

October Term, 1989

Kansas and Missouri, etc., petitioners

v.

Kansas Power & Light Company, et al.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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QUESTION PRESENTED

Whether the rule of *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968), and *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977), precludes proof that a direct purchaser has passed on an overcharge caused by a third party's antitrust violation when the direct purchaser is required by regulation to pass on the full amount of the illegal overcharge to its customers.

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OCTOBER TERM, 1989

No. 88-2109

KANSAS AND MISSOURI, ETC., PETITIONERS

v.

KANSAS POWER & LIGHT COMPANY, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

This brief is submitted in response to the Court's order inviting the Solicitor General to express the views of the United States.

STATEMENT

1. Respondents are public utilities that purchased natural gas from a pipeline company for their own use and for delivery to their customers. They and other purchasers from the pipeline sued the pipeline and five natural gas producing entities; respondents alleged that the pipeline and producers had conspired to inflate prices in violation of Section 4 of the Clayton Act, 15 U.S.C. 15. Respondents sought as damages both the amount of the overcharge and lost profits attributable to the decrease in demand for natural gas resulting from the higher prices.

Petitioners Kansas and Missouri subsequently filed suit against the same defendants as *parens patriae* on behalf of residential consumers who had purchased natural gas from the utilities. See 15 U.S.C. 15c.[1] The cases were consolidated.

2. Defendants countered that the utilities lacked standing to bring an antitrust suit because the utilities had passed on any illegal increase in the price of natural gas to their customers, as assertedly required by applicable state regulations and tariffs filed with state utility commissions. Pet. 4. Consequently, defendants argued, it was the customers who bore the entire burden of any antitrust injury.

The utilities moved for partial summary judgment as to this defense, and the district court granted their motions. It noted that in *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968), this Court held that a direct purchaser is damaged within the meaning of Section 4 of the Clayton Act, 15 U.S.C. 15, to the extent of the overcharge even if it in fact passed on the entire overcharge to its customers. Pet. App. A25-A27. The district court further observed that although *Hanover Shoe* involved the defensive use of a pass-on theory, this Court later held in *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977), that the offensive use of the pass-on theory (by "indirect" purchasers who seek to prove damages) is also barred. Pet. App. A27.

The district court acknowledged that the extent to which the defendants in this case passed on the allegedly illegal

[1] The residential consumers on whose behalf petitioners sued are not limited to respondents' customers, nor do they include the utilities' residential customers in other states.

Petitioners also sued in a representative capacity on behalf of governmental entities that purchased natural gas from the pipeline. That claim is not at issue here.

overcharge was a disputed factual issue, but it concluded that the pass-on defense would be barred even "if the facts establish that the rate systems governing the utilities permitted a total pass-through of any price increase." Pet. App. A33. Although this Court had suggested that a pass on defense might not be barred when an overcharged buyer has a pre-existing "cost[-]plus" contract for a fixed quantity, *Illinois Brick*, 431 U.S. at 736; see *Hanover Shoe*, 392 U.S. at 494, the district court held that this possible exception did not apply in this case because consumer demand for natural gas is governed neither by a fixed-quantity contract nor by anything resembling its "functional equivalent." Pet. App. A34. Recognizing that the utilities' motions for summary judgment "were, in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity," the district court dismissed petitioners' *parens patriae* claims. Pet. App. A38.

In so ruling, the district court relied on *Illinois* v. *Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206 (1988), where a panel of the Seventh Circuit had on "almost identical facts" rejected a similar "pass[-]on" contention. Pet. App. A36. After the district court rendered its decision, the Seventh Circuit granted rehearing en banc in *Panhandle Eastern*. In response, the district court certified to the Tenth Circuit the following question for interlocutory appeal:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who sub-

sequently passed on most or all of the price increase to the citizens of the State?

Pet. App. A41.

3. The court of appeals answered the certified question in the negative. In the court of appeals' view, the reasoning of *Hanover Shoe* and *Illinois Brick* requires that the cost-plus exception – if there is one[2] – be limited to cases involving a pre-existing contract for a fixed quantity. Pet. App. A8. In the absence of a fixed quantity provision, the court reasoned, the utilities would presumably suffer injury from the decreased demand for natural gas resulting from the higher price even if they passed on the entire overcharge. Pet. App. A12-A13. Consequently, it would still be necessary to apportion damages between the direct and indirect purchasers, were the latter permitted to recover. Pet. App. A14. The court of appeals accordingly concluded that even if there were "a perfect and provable pass-on of the allegedly illegal overcharge" in this case, *ibid.*, the cost-plus exception would not apply.

In the meantime, the en banc Seventh Circuit had reached a contrary conclusion in *Illinois* v. *Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (en banc), cert. denied, 109 S. Ct. 543 (1988). The Tenth Circuit, however, expressly declined "to apply the law as enunciated in *Panhandle Eastern*." Pet. App. A13.

DISCUSSION

The existence and scope of any cost-plus exception to the rule precluding antitrust damage suits by indirect purchasers is a recurring question of substantial importance. Uncertainty regarding who may recover an illegal overcharge

[2] The court noted that this Court did not say that a pre-existing cost-plus contract for a fixed quantity "would constitute an exception but rather that it 'might be.' " Pet. App. A8.

undermines the rationale of the *Illinois Brick/Hanover Shoe* rule, which is intended to curtail litigation on that issue and enhance the deterrent value of the treble damage remedy. The court of appeals' construction of the cost-plus exception in this case conflicts squarely with the Seventh Circuit's construction in *Panhandle Eastern*. Accordingly, we urge the Court to grant the petition and clarify the scope of the exception.

We have initiated a comprehensive review of the complex legal and policy questions implicated by this issue among the agencies charged with enforcing the antitrust laws. Although that review is not yet complete, we are convinced that resolution of this troubling issue by this Court would be of substantial benefit to the antitrust litigants, the courts, and the public.

1. In *Hanover Shoe*, this Court – in a case in which the plaintiff claimed damages in the amount of an unlawful monopoly overcharge – rejected the asserted defense that the buyer had passed on the overcharge to its customers. The Court was unwilling to recognize an exception to the established principle that a buyer who has paid an overcharge is injured in the amount of the overcharge "[e]ven if it could be shown that the buyer raised his price in response to, and in the amount of, the overcharge and that his margin of profit and total sales had not thereafter declined." 392 U.S. at 493. It reasoned that permitting the defense that the overcharge was passed on would result in "normally * * * insurmountable" evidentiary problems and "additional long and complicated proceedings," *ibid.*, to establish the effect of an unlawful overcharge on a middleman's prices and profits. Moreover, the Court observed, permitting the defense might leave only ultimate consumers as potential plaintiffs, and yet individual consumers "would have only a tiny stake in a lawsuit and little interest in attempting a class action." *Id.* at 494. Consequently,

"[t]reble-damage actions, the importance of which the Court has many times emphasized, would be substantially reduced in effectiveness," *ibid.*, in deterring violations of the antitrust laws. Notwithstanding its articulated reservations about the wisdom of allowing a pass-on defense, the Court nonetheless recognized that there "might" be situations in which such a defense would be permitted, "for instance, when an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." *Ibid.*

In *Illinois Brick*, an indirect purchaser sought to recover overcharges allegedly passed on to it by a direct purchaser from alleged antitrust violators. The Court held that the rule of *Hanover Shoe* applied equally to this "offensive" use of pass-on in litigation, in large measure because "allowing offensive but not defensive use of pass-on would create a serious risk of multiple liability for defendants." 431 U.S. at 730. Moreover, the Court concluded that the complexity and enforcement rationales of *Hanover Shoe* applied to offensive as well as defensive uses of the pass-on contention.[3] The Court recognized that concentrating the entire recovery in the direct purchaser might leave indirect purchasers without compensation even where they had in fact been injured by an overcharge. But it expressed considerable doubt that permitting indirect purchasers to sue for damages would lead to a recovery accurately reflecting the injury suffered.[4]

[3] The Court observed that "direct purchasers sometimes may refrain from bringing a treble-damages suit for fear of disrupting relations with their suppliers," 431 U.S. at 746, but nevertheless concluded that on balance enforcement objectives would be better served by treating direct purchasers as bearing the entire overcharge than by attempting to apportion that overcharge.

[4] The Court noted that indirect purchasers with a small stake in a lawsuit might not come forward even in a class action. 431 U.S. at 747 & n.31.

The Court in *Illinois Brick* generally rejected "attempts to carve out exceptions to the *Hanover Shoe* rule for particular types of markets," 431 U.S. at 744, observing that "the process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility to proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid," *id.* at 744-745. It did, however, refer to the suggestion in *Hanover Shoe* that there might be an exception for pre-existing cost-plus contracts, explaining that "[i]n such a situation, the purchaser is insulted from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price" so that "[t]he effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand." *Id.* at 736.[5] Thus, although the Court has never held that there is an exception to the pass-on rule for situations involving pre-existing cost-plus, fixed quantity contracts, it has suggested that such an exception exists.[6]

2. The Court's dicta suggesting the existence of a cost-plus exception have led to conflict in the circuits concerning the scope of the exception. In particular, the Tenth Cir-

[5] To the extent that a direct purchaser deals with indirect purchasers pursuant to a preexisting cost plus contract for a fixed quantity, the direct purchaser presumably is fully compensated by the indirect purchasers for his payment of an illegal overcharge and loses no profits as a result of declining sales volume.

[6] The Court's most recent reference to this possible exception in *California v. Arc American Corp.*, 109 S. Ct. 1661, 1663 n.2 (1989), contains no reference to the fixed quantity component of the exception, citing a footnote in *Illinois Brick*, 431 U.S. at 732 n.12, which in turn refers to the Court's earlier discussion in *Hanover Shoe*. The fixed quantity requirement was not explicitly mentioned in *Hanover Shoe*; it was first articulated in *Illinois Brick* itself.

cuit in this case and the Seventh Circuit in *Panhandle Eastern* have come into square conflict with respect to the necessity of a fixed quantity provision.

Panhandle Eastern, like this case, involved natural gas purchased by a utility from a pipeline at prices allegedly inflated by antitrust violations and then resold by the utility to its customers at prices affected by the overcharge. The State of Illinois brought suit on behalf of the utility's customers to recover the passed-on overcharge.[7] The pipeline moved to dismiss Illinois's suit, citing the pass-on rule. The district court denied the motion, but certified the issue for interlocutory appeal. The en banc court unanimously ruled that the utility's industrial purchasers could not sue, but in a divided ruling (six to four) permitted residential customers of the utility to sue.

The Seventh Circuit reasoned that "there is no indication that by using the words 'fixed quantity' the Supreme Court meant to address the issue of the status of regulatory cost-plus pricing." Pet. App. A47. The utility in the case before the Seventh Circuit was required by statute to sell, and did sell, gas subject to a contractual provision requiring it to pass on the full amount of the alleged overcharge to residential customers.[8] There was no fixed quantity provision, but

[7] The utility subsequently also filed suit.

[8] The court noted that it was conceivable that but for the overcharge the utility would have sought and obtained a rate increase and, therefore, that the pass on might not in fact have been complete. It deemed this possibility too insignificant to affect its conclusion, however. Pet. App. A59.

Gas sold to industrial customers was subject to the same contractual provision but, because industrial customers had alternatives to natural gas, the responsiveness of demand to price increases was greater than that of residential customers. The utility therefore sought, and obtained, regulatory permission not to pass the entire amount of the overcharge on to industrial customers. Pet. App. A52.

the Seventh Circuit apparently understood the fixed quantity requirement mentioned by this Court in *Illinois Brick* as intended primarily to assure that the full overcharge would be passed on.[9] Regulation that holds price below the profit-maximizing price, the court reasoned, provides similar assurance, thus rendering the fixed quantity requirement unnecessary. *Id.* at A50-A51.[10] The court acknowledged, however, that although the regulatory context might provide assurance that the overcharge would be fully passed on and make proof of the amount of the injury incurred by indirect residential customers "straightforward," *id.* at A55, it would not preclude injury to the utility resulting from loss of sales at the higher price. Accordingly, the court concluded that the indirect residential customers could recover damages for the overcharge, while the utility could recover damages resulting from lost sales, *id.* at A54, as well as for the overcharge on gas sold to industrial customers.

On similar facts,[11] the Tenth Circuit concluded that only the direct purchaser could sue, flatly rejecting *Panhandle Eastern*, Pet. App. A15, and pointing to "the issue of

[9] As previously noted, however, the fixed quantity provision would also insulate the direct purchaser against the risk of lost sales resulting from a price increase. See note 5, *supra*.

[10] The court apparently viewed requirements contracts as providing similar assurance, using such contracts to illustrate why "a rigid test of fixed quantity would be a senseless limitation on the cost-plus exception." Pet. App. A57.

[11] The Tenth Circuit "distinguish[ed] the facts" of *Panhandle Eastern* from those in this case, Pet. App. A13, but not persuasively. As it observed, *id.* at A14, the most important difference between the two cases relates to the likelihood of a complete pass on of the overcharge, a difference which cannot have affected the result because of the Tenth Circuit's assumption that there was a "perfect and provable pass-on." *Ibid.*

decreased demand due to higher prices," *Id.* at App. A14, as a primary reason for its conclusion. In the Tenth Circuit's view, "[i]f we were to adopt the reasoning of *Panhandle Eastern*, we would in reality be carving out yet another exception * * * to the basic rule that only a direct purchaser may sue for the antitrust violation." *Id.* at A15. The holdings of the Tenth and Seventh Circuits cannot be reconciled.[12]

Nor can this case be reconciled with the Fifth Circuit's disposition of the fixed quantity requirement in *In re Beef Industry Antitrust Litigation*, 600 F.2d 1148, 1164 (1979), cert. denied, 449 U.S. 905 (1980). There the court treated overcharge damages and lost profits due to diminished volume resulting from an overcharge as "wholly separable items of damage," implying that separate suits could be maintained. Thus, at least one panel of the Fifth Circuit appears to share the Seventh Circuit's view of the fixed quantity requirement.[13] The Seventh Circuit, however, characterized the *Beef Industry* formulation as "requir[ing] elaborate analysis of the incidence of a cost increase, which is precisely the analysis that the Court disparaged in *Illinois Brick*," Pet. App. A48, because, in the Seventh Circuit's view, the Fifth Circuit would apply the exception even in the absence of a cost-plus contract, so long as pricing prac-

[12] The Sixth Circuit has also declined to follow *Panhandle Eastern*'s analysis of the fixed quantity requirement, *County of Oakland* v. *City of Detroit*, 866 F.2d 839, 854 (1989) (order denying rehearing), petition for cert. pending, Nos. 89-56, 89-79 and 89-101, in a case involving somewhat different facts. We have filed a brief as amicus curiae in *Allevato* urging the Court to hold those petitions pending the Court's disposition of this case.

[13] An earlier case in the Fifth Circuit had reached a different result. *Yoder Bros.* v. *California-Florida Plant Corp.*, 537 F.2d 1347, 1375-1376 (1976), cert. denied, 429 U.S. 1094 (1977), held that the exception required a showing that the direct purchaser suffered no loss of sales from a higher price.

tices in the market constitute the "functional equivalent" of such a contract.

3. Whether an exception to the rule of *Hanover Shoe* and *Illinois Brick* should be fashioned to take account of the possibility that the direct purchaser may suffer no injury at all and, if so, what limits should be placed on that exception to prevent it from undermining the purposes of the rule, are difficult questions. Answering them requires consideration of the three fundamental and interrelated policy goals identified by this Court: (1) preventing undue complication of antitrust litigation; (2) providing compensation to victims of antitrust violations; and (3) maintaining the treble damage remedy as an effective deterrent to antitrust violations.

Recognizing an exception to the fundamental rule prohibiting proof of a pass-on would inevitably complicate antitrust litigation to some extent, as there would always be potential for litigation about the applicability of the exception in particular circumstances. The risk of complicating litigation would be more significant if the exception encompassed more than preexisting cost-plus contracts providing for a fixed quantity. In particular, dispensing with the requirement of a fixed quantity and allowing indirect purchasers to claim the overcharge while at the same time allowing direct purchasers to claim damages for lost profits attributable to lost sales, would add additional parties to the litigation and could present potentially difficult issues about whether lost sales are attributable to higher charges or to some other factor.[14]

[14] Even more complex litigation would be engendered by a formulation allowing the parties to litigate the extent to which the overcharge actually was passed on, as opposed to a formulation focusing exclusively on the existence of a legally binding provision providing for a complete pass on. We note that the Seventh Circuit viewed proof of the indirect purchasers' loss as "straightforward" in a regulatory context,

On the other hand, an exception where overcharges are fully passed on would probably increase compensation for injured parties. As the Court has noted, the *Hanover Shoe* rule "does further the goal of compensation to the extent that the direct purchaser absorbs at least some and often most of the overcharge." *Illinois Brick*, 431 U.S. at 746. Nevertheless, it seems clear that one consequence of the rule is that at least some indirect purchasers that suffer actual injury will be left uncompensated. Thus, to the extent that no regulatory or other mechanism requires the direct purchaser to pass on the recovery of antitrust damages to indirect purchasers, recognition of an exception allowing indirect purchasers to recover directly where they alone suffer injury would plainly serve the purpose of compensation. Moreover, even if there are regulations requiring direct purchasers to pass on antitrust damages to customers, those regulatory mechanisms, like the litigation mechanisms for recovery by numerous injured parties, may work imperfectly. Conversely, of course, if an exception were recognized for cost-plus contracts and only indirect purchasers are allowed to recover (to avoid the problem of increased complexity and litigation costs), direct purchasers could be left uncompensated.

Finally, an exception could affect the incentives of private plaintiffs—and thus the deterrent value of the remedy—in a variety of ways. As this Court observed in *Illinois Brick*, 431 U.S. at 745-746, dividing the recovery among many potential plaintiffs may dilute the incentive to sue, and therefore undermine the deterrent effect of the treble damage remedy.[15] On the other hand, a direct purchaser

Pet. App. A55, while the Tenth Circuit, on somewhat different facts, rejected petitioners' contention that such proof would be simple, Pet. App. A11-A12.

[15] *Parens patriae* actions, such as this one, may to some extent avoid the problem of multiple potential plaintiffs. However, the states may

who has a cost-plus contract presumably suffers less injury from an antitrust violation than other types of direct purchasers, and thus has less incentive to sue. Similarly, if direct purchasers are required either by regulation or contractual provisions to pass on antitrust recoveries to their customers, they may have a reduced incentive to sue. Compare Pet. App. A50-A51 (public utility commission may force utility to pass recovery on to consumers, leaving utility with no incentive to sue), with Pet. App. A11 (utilities must believe there is benefit in pursuing these actions).

Our review of these policy considerations is ongoing. If the Court grants the petition, we anticipate that we will file a brief discussing the appropriate scope of the cost-plus exception, taking into account each of the foregoing factors.

sue as *parens patriae* only on behalf of natural persons. Moreover, states may face resource constraints that would limit their ability to bring such actions.

CONCLUSION

The petition for a writ of certiorari should be granted.

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In The

Supreme Court of the United States

October Term, 1988

THE STATES OF KANSAS AND MISSOURI, AS *PARENS PATRIAE*,

Petitioners,

v.

THE KANSAS POWER & LIGHT COMPANY,

AND

UTILICORP UNITED, INC.,

Respondents.

BRIEF OF THIRTY-TWO STATES AS AMICI CURIAE ON BEHALF OF PETITIONERS FOR A WRIT OF CERTIORARI

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No. 88-2109

IN THE
SUPREME COURT OF THE UNITED STATES
October Term, 1988

THE STATES OF KANSAS AND MISSOURI,
AS PARENS PATRIAE,

Petitioners,

v.

THE KANSAS POWER & LIGHT COMPANY

and

UTILICORP UNITED, INC.,

Respondents.

BRIEF OF THIRTY-TWO STATES AS AMICI CURIAE ON BEHALF OF PETITIONERS FOR A WRIT OF CERTIORARI

INTRODUCTION

The States of Alaska, Arkansas, California, Colorado, Connecticut, Florida, Hawaii, Illinois, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Minnesota, Nebraska, Nevada, New Hampshire, New Jersey, North Carolina, Ohio, Oregon,

Pennsylvania, South Dakota, Tennessee, Texas, Utah, Virginia, Washington, West Virginia, and Wisconsin (hereinafter "Amici States") submit this brief in support of Kansas' and Missouri's Petition for Writ of Certiorari.

INTERESTS OF THE AMICI STATES

The Attorneys General of the Amici States are the chief law enforcement officers of their states and are charged with the duty of enforcing both state and federal antitrust laws. In their parens patriae capacity, the Amici States, represented by their attorneys general, are authorized to bring federal antitrust actions to recover damages on behalf of the citizens of their states.[1/] The Amici States have a vital interest in preventing the erosion of their parens patriae authority.

1/ 15 U.S.C. § 15c. See also Georgia v. Pennsylvania R.R., 324 U.S. 439 (1945) (common law parens patriae authority).

The States, thus, play a major role in antitrust enforcement and have a substantial interest in ensuring that the antitrust laws are interpreted in accord with sound antitrust policy and the prior decisions of this Court.

The Amici States support the contention of Kansas and Missouri that the instant suit on behalf of residential consumers is within the cost-plus exception to Hanover Shoe, Inc. v. United Shoe Machinery Corp., 392 U.S. 481 (1968) and Illinois Brick Co. v. Illinois, 431 U.S. 720 (1977). Kansas and Missouri assert that the cost-plus exception controls because the federal[2/] and state[3/] regulation of natural gas utilities creates a

2/ See the Natural Gas Act, 15 U.S.C. § 717 et seq. (1982) and the Natural Gas Policy Act, 15 U.S.C. § 3301 et seq. (1982).

3/ See Kan. Stat. Ann. §§ 66-1,201, 66-1,206 (1985); Mo. Rev. Stat. §§ 368.250(5), 393.140(1), 393.270(2) (1986).

cost-plus pricing arrangement, passing on all of the increased cost of gas to the consumer.[4/]

The Tenth Circuit Court of Appeals rejected Kansas' and Missouri's contention, holding that the states could not bring a parens patriae action on behalf of their residential consumers who were indirect purchasers of the natural gas. See In re Wyoming Tight Sands Antitrust Cases, 866 F.2d 1286, 1294 (10th Cir. 1989) (reprinted in Appendix A of the Petition for Writ of Certiorari). In so holding, the Tenth Circuit weakened antitrust law by depriving injured residential consumers of relief and by creating a split between the circuits.

4/ Many of the Amici States have also enacted statutes that cause costs of natural gas production to be passed through to the ultimate consumers. See, e.g., Conn. Gen. Stat. § 16-196 (1989); Md. Code Ann. art. 78 § 54D (1980 Repl. Vol.); Ohio Rev. Code § 4905.302 (Supp. 1988); 66 Pa. Cons. Stat. Ann. § 1307(f) (1984); Va. Code § 56-235 (1986 Repl. Vol.).

SUMMARY OF ARGUMENT IN FAVOR OF GRANTING THE WRIT

1. The Tenth Circuit's decision deprives overcharged residential consumers who purchase products pursuant to a regulatory cost-plus contract of the right to sue for injury they have clearly suffered. It also deprives them of the most appropriate counsel to represent their collective interests--State attorneys general. This Court should resolve the substantial issues raised in this case regarding the States' parens patriae authority.

2. The Tenth and Seventh Circuits have reached opposite results when faced with the same set of material facts: an illegal price fixing conspiracy by producers of natural gas sold to residential consumers pursuant to a regulatory cost-plus arrangement. This Court should resolve the conflict between the circuits.

3. The Seventh Circuit's en banc decision, in Illinois v. Panhandle Eastern Pipe Line Co., 852 F.2d 891 (7th Cir.) (en banc), cert. denied, 109 S. Ct. 543 (1988), comports with sound antitrust policy.

Moreover, on the facts presented in both that case and the instant case, the Seventh Circuit's decision properly reconciles the policy set forth by this Court in Illinois Brick with the intent of Congress in enacting the Hart-Scott-Rodino Antitrust Improvements Act of 1976.

ARGUMENT IN FAVOR OF GRANTING THE WRIT

I.

THE TENTH CIRCUIT'S DECISION RAISES SUBSTANTIAL ISSUES REGARDING THE STATES' PARENS PATRIAE AUTHORITY.

Title III of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (hereinafter "Hart-Scott-Rodino")[5/] empowers State attorneys general to enforce the federal antitrust laws by representing their resident natural persons.[6/] Throughout the

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5/ Pub. L. No. 94-435, 90 Stat. 1383 (1976). Title III added sections 4C through 4H to the Clayton Act, 15 U.S.C. §§ 15c through 15h.

6/ Congress conferred this parens patriae authority in response to California v. Frito-Lay, Inc., 474 F.2d 774 (9th Cir. 1973), cert. denied, 412 U.S. 908 (1973). In (Continued)

thirteen years since its creation, the States' parens patriae authority has been a powerful and effective weapon against antitrust wrongdoing.[7/] Courts have recognized the superiority of the parens patriae action as a tool for representing the collective claims of a

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Frito-Lay, the Ninth Circuit held that the state could not maintain an action as parens patriae on behalf of citizen-consumers to recover monetary damages for injuries suffered from an alleged price-fixing conspiracy among snack food manufacturers. 474 F.2d at 777. The court recognized that California had advanced what was "perhaps the most suitable" answer to deal with the problem of antitrust deterrence, but declined to usurp the power of the legislative branch. Id.

7/ See, e.g., In re Panasonic Consumer Electronics Antitrust Litigation (Civ. Action No. 89 Civ. 0368 (SWK)) (S.D.N.Y. 1989) ($16 million parens settlement available for 665,000 consumers obtained by 49 States and the District of Columbia); In re Minolta Camera Products Antitrust Litigation, 668 F. Supp. 456 (D. Md. 1987) ($4 million parens settlement available for over 300,000 consumers obtained by 36 states and the District of Columbia); Connecticut v. Waldbaum, Inc., Dkt. No. H-87-263 (D. Conn. 1987); Connecticut v. Stop & Shop Co., Inc., Dkt. No. H-86-688 (D. Conn. 1988) (in settlement of related parens cases, coupons valued at $21 million obtained for Connecticut consumers); In re Mid-Atlantic Toyota Antitrust Litigation, 605 F. Supp. 440 (D. Md. 1984) ($5 million parens settlement for over 35,000 consumers obtained by five States and the District of Columbia).

State's citizens.[8/] Indeed, "it is difficult to imagine a better representative of the retail consumer within a State than the State's Attorney General." In re Ampicillin Antitrust Litigation, 44 F.R.D. 269, 274 (D.D.C. 1972); See also In re Antibiotic Antitrust Actions, 333 F. Supp. 278, 280 (S.D.N.Y. 1971).

The decision below deprives residential consumers of a remedy for the overcharges they paid. In any event, the damage suffered by any given consumer is too small to justify substantial expenditure of time and money in protracted litigation. This is precisely the type of lawsuit that the parens patriae provisions were designed to permit.

In addition, public utility commissions may require regulated utilities to pass recoveries from

8/ "The parens patriae action is plainly superior to the [Rule 23] class action as a mode for adjudication of collective claims." In re Montgomery County Real Estate Antitrust Litigation, 1988-2 Trade Cas. (CCH) ¶ 68,230 (D. Md. 1978). See also Pennsylvania v. Budget Fuel Co., 1988-2 Trade Cas. (CCH) ¶ 68,229 (E.D. Pa. 1988).

lawsuits on to residential consumers. As a result, regulated utilities may have "no incentive to sue because they will have nothing to gain from the suit." Panhandle Eastern, 852 F.2d at 895. Thus, unless State attorneys general are allowed to represent residential consumers in these cases, price fixers may elude justice.

State attorneys general have the incentive, and the experienced, specialized antitrust counsel, to prosecute these suits vigorously on behalf of their citizens. This Court should permit these injured residential consumers to obtain representation by their State attorneys general.

II.

THE SEVENTH AND TENTH CIRCUITS ARE IN CONFLICT REGARDING THE EXISTENCE OF THE REGULATORY COST PLUS EXCEPTION TO ILLINOIS BRICK

The facts before the Seventh Circuit in Panhandle Eastern and before the Tenth Circuit in the

instant case are similar in all material respects.[9/] In both cases, the State attorneys general brought suit as parens patriae on behalf of residential consumers who purchased natural gas from regulated utility companies that had passed along all overcharges caused by producers' illegal price fixing.[10/] The Seventh Circuit

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9/ Indeed, the district court opinion stated that the Panhandle Eastern case and the instant case have "almost identical facts." In re Wyoming Tight Sands Antitrust Cases, 695 F. Supp. 1109, 1117 (D. Kan. 1988). The appellate court's effort to distinguish this case from Panhandle Eastern fails. The purported distinctions it draws are not based on factual differences but upon the ground that facts present in Panhandle Eastern "may or may not" be present here. The court noted that there "may" be formal cost-plus pricing in this case. App. A, A 13-14. The court further noted that in this case the 100% pass-on in Panhandle Eastern "may or may not" be present here. Id. at 14. Yet the state statutes in Panhandle Eastern and the regulations in the instant case are nearly identical. Both require a 100% pass on. See footnote 10.

10/ In Panhandle Eastern, the court found that the full amount of the illegal overcharge was passed on to residential consumers. 852 F.2d at 892. In the instant case, the Circuit Court "assumed that there was a perfect and provable pass-on of the illegal overcharge. . . ." App. A, A8-13. In fact, the regulatory schemes in effect in Illinois, Kansas, and Missouri require regulated utilities to pass price increases from suppliers on to their residential
(Continued)

allows residential consumers to recover damages from gas producers that fix prices under the "cost-plus" exception stated in Illinois Brick Co. v. Illinois, 431 U.S. 720, 735-36 (1977), but the Tenth Circuit does not.

The conflict between the Circuits centers on whether a cost-plus exception is available when the regulatory scheme does not require consumers to purchase a fixed quantity from the utility.[11/] In the instant case, the court below construed the cost-plus exception in Illinois Brick to require a contract for a fixed quantity. As it is highly impractical for consumers to contract for a fixed quantity of natural

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consumers. See Panhandle Eastern, 852 F.2d at 895; Petition for Writ of Certiorari at 4 n.3.

11/ Petitioners advance a claim only on behalf of residential consumers of the regulated product. First, Hart-Scott-Rodino limits State attorneys general parens patriae lawsuits to those on behalf of "natural persons." 15 U.S.C. § 15c. Second, the Seventh Circuit in Panhandle Eastern determined that industrial customers should not be allowed to sue for damages because a different and more difficult apportionment of damages would be necessary. 852 F.2d at 898.

gas, the cost-plus exception was deemed inapplicable. App. A, A 12-13.

The Panhandle Eastern court held that a fixed quantity provision was not an essential condition for the cost-plus exception when dealing with a regulated industry.[12/] The court found that a fixed quantity provision in a cost-plus contract allows the direct purchaser to maximize its profits. It may pass on the full overcharge because its buyer must purchase the quantity of goods stated in the contract. Similarly, the presence of regulation and mandatory pass-on provisions allows regulated utilities to maximize profits from residential consumers by passing on the

12/ The court stated that the term "fixed quantity" in Illinois Brick was related to the facts in that case: a requirements contract for the purchase of unlimited quantities of one of a large number of building components. "Certainly there is no indication that the Supreme Court meant to address the issue of regulatory cost-plus pricing [in Illinois Brick]" 852 F.2d at 893. The court added the common sense observation that "we do a disservice to the Court by wrenching its words out of context and giving them talismanic significance; we make language a trap rather than a mode of communication." Id.

full overcharge to them.[13/] Thus, the court held that regulation is a "stand in" for the fixed quantity requirement. 852 F.2d at 896.

This Court should resolve the conflict between the circuits so that all States will be able to utilize the cost-plus exception in regulatory cases.

III.

THE DECISION OF THE SEVENTH CIRCUIT IS CONSISTENT WITH BOTH ILLINOIS BRICK AND THE STATES' PARENS PATRIAE AUTHORITY

The Seventh Circuit's decision in Panhandle Eastern recognizes the injustice that would result from the dismissal of this type of parens patriae lawsuit.[14/] Moreover, it reconciles Illinois Brick with

13/ In both this case and Panhandle Eastern, the regulatory schemes require passing on of increased gas prices. See Petition for a Writ of Certiorari at pp. 4, 9.

14/ "[T]he doubts here are too small to warrant our insisting that this potentially serious antitrust violation, which may have caused consumers to pay almost $50 million in higher prices, shall go unremedied, as it may if we accept [the pipeline's] view of the scope of Illinois Brick." Panhandle (Continued)

the intent of Congress in Hart-Scott-Rodino.

A.

REGULATORY COST-PLUS CONTRACTS ELIMINATE THE COMPLEXITY AND DAMAGE APPORTIONMENT CONCERNS OF ILLINOIS BRICK

The court below noted the Illinois Brick Court's concern that permitting indirect purchasers to seek damages would introduce undue complexity into already complex antitrust litigation. The court stated that allowing states to pursue parens patriae claims would complicate proof of damages by adding "unnecessary issues." App. A, A10. In this, the lower court disregarded congressional intent to permit courts to deal with the complexities inherent in parens patriae cases. Nevertheless, in light of the pass-on, apportioning damages in this case will be much less complex than it would have been in Illinois Brick.

By contrast, the Panhandle Eastern court was not troubled by problems of calculation and apportionment

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Eastern, 852 F.2d at 898.

of damages. It stated that a "cost-plus" contract obviates the problem of apportioning damages because the whole of any price increase has been passed on to the indirect purchaser. 852 F.2d at 894, 896-97. See also California v. ARC America Corp., 109 S. Ct. 1661, 1666 n.6 (1989) ("indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them").

Apportioning damages in this case is easy. Because the utility is a monopolist, it could charge consumers a higher price but for the existence of regulation. Thus, the utility possesses "unused monopoly power" and can require residential customers to pay the whole overcharge. 852 F.2d at 895. As a result, it is not significantly more difficult to apportion injury in this situation than it is to calculate the injury suffered by the direct purchaser.[15/]

15/ One of the rationales given by the Tenth Circuit for refusing to recognize a regulatory cost-plus (Continued)

B.

THE STATES ARE THE BEST PLAINTIFFS TO SUE ON BEHALF OF RESIDENTIAL CUSTOMERS IN REGULATORY COST-PLUS CASES

The court below noted that this Court in Illinois Brick made a policy judgment that direct purchasers should be encouraged to sue by offering them the incentive of recovering all the damages they sustained. The court stated that permitting the States to bring these parens patriae cases would reduce this incentive and would shift "the cost and incentive of policing and enforcing the antitrust laws to the states." App. A, A10. The court's perspective is totally at odds with the concerns of Congress. In Hart-Scott-Rodino, Congress decided that in cases

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exception is the difficulty of calculating the extent to which indirect purchasers mitigated damages by seeking alternate energy sources. App. A, A 12. However, Panhandle Eastern directly addressed this contention. Even if the total amount of gas sold were lowered because of the conspiracy, consumers are still injured by the overcharges paid for the units they did purchase. 852 F.2d at 896. Residential consumers were not seeking to recover for items of expense beyond the overcharge.

where natural persons (residential consumers) are injured, the cost and burden of representing these citizens should shift to the States.[16/]

The Seventh Circuit's opinion is consistent with this Court's recent decision in California v. ARC America Corp., 109 S. Ct. 1661 (1989) which recognized that indirect purchasers could, in certain instances, be better antitrust enforcers than direct purchasers. Pointing to its decision in Illinois Brick, this Court stated:

> Indeed, we implicitly recognized as much in noting that indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them. See 431 U.S. at 732 n.12.

109 S. Ct. at 1666 n.6. A regulatory cost-plus contract is one of those instances. See Petition for Writ of Certiorari at pp. 10-13.

16/ Regulated utilities have little incentive to prosecute antitrust claims on behalf of residential consumers. See pp. 8-9, supra. Thus, the need for State attorneys general to represent their citizens is particularly important in cases of regulatory pass-ons.

C.

THE VIEW OF THE SEVENTH CIRCUIT IS CONSISTENT WITH ILLINOIS BRICK AND THE INTENT OF CONGRESS

The Seventh Circuit's decision in Panhandle Eastern comports with both the policies of Illinois Brick and the parens patriae provisions of Hart-Scott-Rodino. The court recognized that permitting an action on behalf of residential purchasers of natural gas pursuant to regulatory cost-plus pricing did not offend the policies articulated in Illinois Brick. Further, the Seventh Circuit also permitted the Attorney General of Illinois to act in the manner authorized by Hart-Scott-Rodino. The parens patriae suit allowed the Attorney General to protect the residential consumers of his State and to ensure vigorous enforcement of the antitrust laws.

In contrast, the decision of the Tenth Circuit ignores the public policy concerns of Illinois Brick. Moreover, by expressing concern that Kansas and Missouri sought to "shift" the responsibility of

prosecuting antitrust cases on behalf of their citizens, the lower court subverts the important goals of Hart-Scott-Rodino. This decision hampers the ability of attorneys general to maintain suit when numerous citizens have been injured. Yet, Congress enacted Hart-Scott-Rodino to permit this type of suit. For these reasons, as well as those articulated by the Seventh Circuit in Panhandle Eastern, the decision of the Tenth Circuit should be overturned.

CONCLUSION

For the foregoing reasons this Court should grant the petition of Kansas and Missouri for a Writ of Certiorari.

DATED: July 24,1989

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October Term, 1989

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AS *PARENS PATRIAE*,

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vs.

THE KANSAS POWER & LIGHT COMPANY
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On Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

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04/12/85	60	Complaint of Intervening Plaintiff Missouri Public Service Company

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07/11/88	555	ORDER ENTERED TENTH CIRCUIT COURT OF APPEALS: The petitions of the States of Missouri and Kansas for permission to appeal are granted. The appeals are consolidated and assigned Misc. #'s 88-8042 – State of Kansas & 88-8043 – State of Missouri.

UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

DATE	PROCEEDINGS
08/17/88	Joint Appellants' Brief filed by States of Kansas and Missouri
08/17/88	Joint Addendum filed by Appellants
09/19/88	Appellee's Brief filed by Utilicorp United, Inc.
09/20/88	Appellee's Brief filed by Kansas Power & Light Company
09/20/88	Joint Addendum filed by Appellees
01/31/89	Tenth Circuit Opinion filed
2/14/89	Joint Petition for Rehearing filed by Appellants
03/27/89	Order Denying Rehearing

UNITED STATES SUPREME COURT

06/26/89	Petition for Writ of Certiorari filed by States of Kansas and Missouri
1/16/90	Order Granting Certiorari

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

IN RE WYOMING TIGHT) Case No. 85-2349 and
SANDS ANTITRUST CASES) Consolidated Cases

MOTION TO STRIKE, OR, IN THE ALTERNATIVE, FOR PARTIAL SUMMARY JUDGMENT

Plaintiff, The Kansas Power and Light Company ("KPL"), moves the Court to strike as insufficient, pursuant to Fed. R. Civ. P. 12(f), or, alternatively pursuant to Fed. R. Civ. P. 56, for partial summary judgment on, defenses[1] raised to the antitrust claims of KPL's Third Amended Complaint. These defenses raise the standing and scope-of-injury issues commonly called the "pass-on" defense under Section 4 of the Clayton Act, 15 U.S.C. § 15. Defendants allege that KPL lacks standing or has not sustained injury under Section 4 because KPL, the direct purchaser of the illegally-priced gas at the center of this action, passes on most gas costs to its customers.

The United States Supreme Court and numerous Courts of Appeals have soundly rejected the pass-on defense. The reasoning underlying KPL's alternative

[1] The challenged defenses are set out in Exhibit A to the supporting memorandum submitted herewith. They are: Fourth Defense, Answer of Cities Service Oil and Gas Corporation and CSG Exploration Company to KPL's Third Amended Complaint, at 22 (filed July 31, 1987); Seventh and Ninth Affirmative Defenses, Answer of Amoco Production Company to KPL's Third Amended Complaint, at 62 (filed July 31, 1987); and Fourth and Seventeenth Affirmative Defenses, Answer of Williams Natural Gas Company to KPL's Third Amended Complaint, at 23 and 25 (filed July 31, 1987).

motion to strike or for partial summary judgment is set forth in the accompanying supporting memorandum.

KPL submits that this issue is ripe for resolution pursuant to either Rule 12(f) or Rule 56. KPL's summary judgment motion is timely filed. While KPL's alternative 12(f) motion is not filed within twenty (20) days of defendants' answers to the Third Amended Complaint of KPL, the Court may strike an insufficient defense at any time, and thus may consider untimely motions to strike. KPL requests that the Court consider KPL's motion to strike together with that of co-plaintiff Utilicorp United, Inc., which timely filed its motion raising the same issue.

Respectfully submitted,

[Signatures Omitted in Printing]

EXHIBIT A

DEFENDANTS' CHALLENGED DEFENSES

I. *ANSWER OF CITIES SERVICE OIL AND GAS CORPORATION AND CSG EXPLORATION COMPANY TO KPL'S THIRD AMENDED COMPLAINT*, at 22 (filed July 31, 1987).

Fourth Defense

Plaintiff lacks standing to sue under the antitrust laws and under the Racketeer Influenced and Corrupt Organizations Act.

II. *ANSWER OF AMOCO PRODUCTION COMPANY TO KPL'S THIRD AMENDED COMPLAINT*, at 62 (filed July 31, 1987).

Seventh Defense

The Third Amended Complaint is barred because plaintiff lacks standing to bring this action.

Ninth Defense

The Third Amended Complaint is barred because plaintiff has not been injured in its business or property by reason of anything forbidden by the antitrust laws of the United States or the Racketeer Influenced and Corrupt Organizations Act.

III. *ANSWER OF WILLIAMS NATURAL GAS COMPANY TO KPL'S THIRD AMENDED COMPLAINT*, at 23 and 25 (filed July 31, 1987).

Fourth Affirmative Defense

For a Fourth Affirmative Defense, [WNG] alleges that plaintiff lacks standing to bring all or some of the claims in this action.

Seventeenth Affirmative Defense

For a Seventeenth Affirmative Defense, [WNG] alleges that plaintiff has not been injured in its business or property by reason of anything forbidden in the antitrust laws of the United States or any state.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

IN RE WYOMING TIGHT SANDS ANTITRUST CASES	) Case No. 85-2349 S and) Consolidated Cases

KPL'S STATEMENT OF MATERIAL FACTS
WHICH ARE NOT IN DISPUTE

1. At all times relevant to this action, plaintiff The Kansas Power and Light Company ("KPL") purchased and continues to purchase natural gas directly from Williams Natural Gas Company, (formerly Cities Service Gas Company and Northwest Central Pipeline Corporation; hereinafter "Pipeline").

2. KPL purchases natural gas directly from Pipeline for its own use and for re-sale to its residential, commercial and industrial customers. Pipeline sends invoices for these purchases to KPL and KPL pays for all such purchases directly to Pipeline.

3. KPL has not had, nor does it currently have, fixed quantity contracts with any of its residential, commercial or industrial customers.

4. Many of KPL's industrial customers can switch from KPL to alternative energy sources or curtail their natural gas usage if dissatisfied with the price, terms or conditions of service offered by KPL.

[Signatures and Certificate of
Service Omitted in Printing]

(8)

No. 88-2109

In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI, AS *PARENS PATRIAE*,

Petitioners,

v.

THE KANSAS POWER & LIGHT COMPANY and UTILICORP UNITED, INC.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

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QUESTIONS PRESENTED

1. Do residential indirect purchasers of natural gas, represented *parens patriae* by their state attorneys general, have standing to sue under Section 4 of the Clayton Act, where there is an easily-proved, 100% pass-on of illegal overcharges, effected by federal and state regulation rather than by a fixed-quantity cost-plus contract?

2. Where federal and state regulations require that the full amount of any illegal overcharge be passed on by the direct purchaser in readily-identifiable form, is there an exception to the general rule barring indirect purchaser antitrust suits under Section 4 of the Clayton Act?

PARTIES

Petitioners, the States of Missouri and Kansas, acting as *parens patriae* on behalf of their residential gas consumers, are two of the six plaintiffs in consolidated litigation known as *In re Wyoming Tight Sands Antitrust Cases*. The States were appellants in the Tenth Circuit proceeding from which this petition arises.

Appellees in the Tenth Circuit included plaintiff The Kansas Power & Light Company ("KPL"), intervenor UtiliCorp United, Inc. ("UtiliCorp," which includes its two subsidiaries, Missouri Public Service Company and Kansas Public Service Company), and plaintiff Kansas Gas & Electric Company ("KG&E"). Plaintiff Farmland Industries, Inc. did not take part in the Tenth Circuit appeal. Because the issues raised in this case do not affect KG&E[1] or Farmland, only KPL and UtiliCorp are named as respondents herein.

Defendants below were Amoco Production Company ("Amoco"), Cities Service Oil & Gas Corporation ("Cities Service"), CSG Exploration Company ("CSGE"), Williams Natural Gas Company ("Pipeline") and two limited partnerships, Moxa Limited Partnership and Wamsutter Limited Partnership. Amoco, Cities Service and CSGE intervened at the Tenth Circuit, but did not take a position as to which group of plaintiffs should prevail. The other defendants did not appear in the Tenth Circuit. None of the defendants is named as a respondent herein.

---

[1] Plaintiff Kansas Gas & Electric is solely an electric utility that does not resell gas. The States did not oppose KG&E's motion for partial summary judgment.

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No. 88-2109

In The

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Petitioners,

v.

THE KANSAS POWER & LIGHT COMPANY and UTILICORP UNITED, INC.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

BRIEF FOR THE PETITIONERS

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. Al-A17) is reported at 866 F.2d 1286. The opinion of the district court (Pet. App. A22-A39) is reported at 695 F. Supp. 1109. The district court's opinion on the motion for certification (Pet. App. A40-A42) is reported at 695 F. Supp. 1119.

JURISDICTION

The judgment of the court of appeals (Pet. App. A20-A21) was entered on January 31, 1989, and a petition for rehearing was denied on March 27, 1989 (Pet. App. A18-A19). A petition for a writ of certiorari was filed on June 26, 1989 (J.A. 7). The petition was granted on January 16, 1990 (*id.*). The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTES INVOLVED IN THE CASE

Section 4 of the Clayton Act, 38 Stat. 731, 15 U.S.C. § 15(a) (1982), provides in pertinent part:

> [A]ny person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

Title III of The Hart-Scott-Rodino Antitrust Improvements Act of 1976 provides in pertinent part:

> Any attorney general of a State may bring a civil action in the name of such State, as parens patriae on behalf of natural persons residing in such State, in any district court of the United States having jurisdiction of the defendant, to secure monetary relief as provided in this section for injury sustained by such natural persons to their property by reason of any violation of sections 1 to 7 of this title. The court shall exclude from the amount of monetary relief awarded in any such

> action any amount of monetary relief (A) which duplicates amounts which have been awarded for the same injury, or (B) which is properly allocable to (i) natural persons who have excluded their claims pursuant to subsection (b)(2) of this section, and (ii) any business entity.

90 Stat. 1394, 15 U.S.C. § 15c(a)(1) (1982).

* * *

> In any action under section 15c(a)(1) of this title, in which there has been a determination that a defendant agreed to fix prices in violation of sections 1 to 7 of this title, damages may be proved and assessed in the aggregate by statistical or sampling methods, by the computation of illegal overcharges, or by such other reasonable system of estimating aggregate damages as the court in its discretion may permit without the necessity of separately proving the individual claim of, or amount of damage to, persons on whose behalf the suit was brought.

90 Stat. 1395, 15 U.S.C. § 15d (1982).

* * *

> Monetary relief recovered in an action under section 15c(a)(1) of this title shall –
>
> (1) be distributed in such manner as the district court in its discretion may authorize; or
>
> (2) be deemed a civil penalty by the court and deposited with the State as general revenues; subject in either case to the requirement that any distribution procedure adopted afford each person a reasonable opportunity to secure his appropriate portion of the net monetary relief.

90 Stat. 1395, 15 U.S.C. § 15e (1982).

STATEMENT OF THE CASE

A. Background

In 1984, 1985 and 1986, the Attorneys General for the petitioners States of Kansas and Missouri ("the States") and three utilities filed complaints charging defendant Williams Natural Gas Company ("Pipeline") and others with selling natural gas at artificially inflated prices. Doc. No. 1,[2] Case No. 85-2364-S, Kansas Complaint; Doc. No. 1, Case No. 86-2351-S, Missouri Complaint.[3] The inflated prices, plaintiffs allege, were the result of a price-fixing conspiracy and other anticompetitive behavior involving Pipeline, its then-parent Cities Service Company, CSG Exploration, Amoco and two limited partnerships. The general background of the conspiracy is described in *Midwest Gas Users Association v. FERC*, 833 F.2d 341 (D.C. Cir. 1987).

The price-fixed gas was produced in Wyoming, then transported by Pipeline and sold to KPL, UtiliCorp and other utilities in Missouri and Kansas.[4] The utilities

[2] References to "Doc. No. ___" are to the list of relevant docket entries in the Joint Appendix.

[3] The States' complaints contain two types of claims against the defendants under state and federal law: claims on behalf of state agencies, municipalities and other political subdivisions, and *parens patriae* claims under 15 U.S.C. § 15c on behalf of indirect-purchaser residential consumers of natural gas. Only the *parens patriae* claims are before this Court.

[4] KPL and UtiliCorp are two of more than 50 gas utilities operating as regulated monopolies within defined service areas in Kansas and Missouri. Other non-party utilities provide natural gas purchased from the conspirators to over 50,000 Kansas residential consumers. The claims of these residential users will be lost if the Attorneys General cannot represent them in their *parens patriae* capacity.

resold the gas to various consumers, including individual residents of the two states. These gas sales occurred under a regulatory system that required *all* gas costs to be passed on by the Pipeline, through the utilities, to the end-use consumers.[5] This regulatory pass-through mechanism is *mandatory;* at no level of distribution is there any discretion to absorb or modify any increase in the cost of gas. Exhibit D to Doc. No. 485.

The effect of this pass-through on the cost of gas to consumers is easy to determine – the utilities make public filings showing the volume and price of gas sold to each customer category, including residential consumers. Exhibit K to Doc. No. 485. Further, the passed-on prices are reflected as a separate identifiable entry on each residential consumer's monthly gas bill from the utilities.

[5] This regulatory mechanism operates first at the federal level, where the Pipeline is regulated by the Federal Energy Regulatory Commission (FERC), pursuant to the Natural Gas Act, 15 U.S.C. §§ 717 *et seq.* (1982) (NGA), and the Natural Gas Policy Act, 15 U.S.C. §§ 3301 *et seq.* (1982) (NGPA). Under the NGA, Pipeline must adjust its rates semiannually to reflect any changes in the price of gas paid to producers by Pipeline, in accordance with Purchased Gas Adjustment (PGA) clauses in Pipeline's tariff. 15 U.S.C. § 717(d), (e); *see* 18 C.F.R. §§ 154.1 *et seq.* (1988).

At the state level, utilities such as KPL and UtiliCorp are regulated by the Missouri Public Service Commission and the Kansas Corporation Commission. *See* Mo. Rev. Stat. §§ 386.250 (5), 393.140(1), 393.270(2) (1986 & Supp. 1989); Kan. Stat. Ann. §§ 66-1,201, 66-1,206 (1985 & Supp. 1989). Both state commissions enforce PGA clauses in the utilities' tariffs. UtiliCorp's Kansas Public Service subsidiary operated under a PGA clause in a locally-enforced municipal ordinance. These PGAs require that KPL and UtiliCorp automatically pass on to their customers the utilities' entire wholesale cost of gas from the Pipeline.

This separate entry (entitled "Wholesale Gas Cost" on KPL's bills) is defined as the amount per customer "for the cost of gas to [KPL]." Appendix H to Doc. No. 474. The amount of any overcharge to the residential consumer is thus the *same* as the amount of the overcharge to the utility, and KPL has recognized as much. *See* pp. 13-14, *infra;* Exhibit D to Doc. No. 485, pp. 2-3.

The Tenth Circuit, recognizing the effect of this regulatory system, assumed for purposes of its decision "that there was a perfect and provable pass-on of the allegedly illegal overcharge. . . ." Pet. App. A14.

B. Proceedings Below

The utilities, in motions for partial summary judgment, argued to the district court that they alone were the proper plaintiffs and that the States lacked standing to sue as *parens patriae* on behalf of the residential consumers because the consumers are indirect purchasers whose claims are barred by the rule of *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968), and *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). Doc. Nos. 440, 448, 458; J.A. 8-9, 12.[6] Although the utilities did not deny that they passed on all of the overcharges to the residential consumers, they argued that because they had

[6] KPL's motion to strike or, in the alternative, for summary judgment, and its statement of uncontroverted facts, are printed in the Joint Appendix. In all relevant respects, the motions and statements of fact filed by UtiliCorp and KG&E are identical. *See* Doc. Nos. 439, 440, 458, 460.

no fixed-quantity contracts with these consumers, no exception to the direct-purchaser rule applied. *Id.* Petitioners countered that because state and federal regulation resulted in an easily-provable and perfect pass-through of all illegal overcharges, they had standing to sue under the *Illinois Brick* exception. Doc. Nos. 474, 485. The district court granted summary judgment in favor of the utilities, holding that even proof of a perfect pass-on would not give the States standing, because there were no "fixed-quantity contracts." Pet. App. A33-34.

On interlocutory appeal, the Tenth Circuit affirmed the district court's dismissal of the States' *parens patriae* claims. While recognizing that "there might be" an exception to the *Hanover Shoe* and *Illinois Brick* rule that only direct purchasers have standing to sue, Pet. App. A7-A8, the Tenth Circuit found no exception applicable here. Even though it assumed a perfect pass-through of damages to the consumer, *id.* at A14, the court narrowly interpreted *Illinois Brick* as *requiring* any exception to the direct-purchaser rule to be based on a pre-existing, cost-plus contract *for a fixed quantity. Id.* at A8. The court of appeals held that no "fixed-quantity contract" was present in this case: "To say that the utilities have a cost-plus fixed fee contract for a fixed quantity with their residential consumers would amount to fitting a square peg into a round hole. There exists no contract between the utilities and their residential consumers for any particular quantity." *Id.* at A12.

The court concluded that even *considering* proof of a perfect pass-on would " 'entail the very problems that the *Hanover Shoe* rule was meant to avoid.' *Id.* at [431 U.S.]

744-45. We therefore hold that the amount of illegal overcharges actually passed on by the utilities to its [sic] customers is not an issue of material fact necessary to a resolution of the narrow issue before this court." Pet. App. A17.

The Tenth Circuit also concluded that this Court's decision in *Illinois Brick* limited *parens patriae* authority under the Hart-Scott-Rodino Act, 15 U.S.C. § 15c, to direct-purchaser suits. Pet. App. A7 n.1.

The court thus affirmed the order of the district court dismissing the States' *parens patriae* actions. As matters now stand, the utilities will be entitled to recover for their own benefit all of the antitrust overcharges, even though these overcharges were fully passed on to the consumers.

SUMMARY OF THE ARGUMENT

The direct-purchaser rule of *Illinois Brick* should not apply here to bar the claims of residential consumers of natural gas. Not only do the present facts meet all this Court's concerns about allowing indirect purchasers to sue, they also fit squarely within the "cost-plus" exception to the rule already recognized by the Court.

This case cannot become the complex battle over apportionment of damages that the Court faced in *Illinois Brick*. Here the overcharges paid by the "middlemen" utilities were passed on in full to the consumers. Proving the amount of the overcharges borne by the consumers is straightforward – the utilities' public filings show the

aggregate price and volume of gas passed on to residential consumers.

The Court's concerns in *Illinois Brick* about finding parties with incentive to sue and encouraging compensation to injured parties are also satisfied by the present facts. The residential consumers, represented *parens patriae* by their state attorneys general, are best suited to recover the antitrust overcharges. The utilities clearly are not. If the utilities are able to recover all overcharges for their own benefit, the injured consumers will not be compensated. But if the utilities are required to turn over any recovered overcharges to the residential consumers, the utilities will lack incentive to prosecute this case vigorously to a conclusion. Only the state attorneys general have both a demonstrated incentive to sue and an interest in compensating the persons actually injured.

The present facts also satisfy the exception to the direct-purchaser rule previously suggested by the Court. The utilities' pricing scheme here is a classic "pre-existing cost-plus contract" under which one would expect all overcharges to be passed on to the indirect purchasers. Moreover, all overcharges here *were* passed on in their entirety.

There is a separate ground for allowing the instant *parens patriae* claims. The Hart-Scott-Rodino Antitrust Improvements Act of 1976 specifically authorizes such suits, without regard to whether state attorneys general are representing direct or indirect purchasers. In fact, the most likely use of the 1976 Act is on behalf of *indirect* purchasers such as the injured residential consumers in this case. Because *Illinois Brick* was not a *parens patriae*

case, this Court has not yet determined whether the Act specifically authorizes *parens* actions such as the present one on behalf of indirect purchasers.

The state attorneys general should be allowed to maintain the present case *parens patriae* on behalf of the parties who sustained the entire antitrust overcharge in easily-provable form – the residential consumers of natural gas.

ARGUMENT

I. RESIDENTIAL CONSUMERS OF NATURAL GAS SHOULD BE ALLOWED TO RECOVER ILLEGAL OVERCHARGES DIRECTLY FROM THE NATURAL GAS PRODUCERS AND PIPELINES THAT VIOLATED THE ANTITRUST LAWS WHERE THE "MIDDLEMEN" UTILITY COMPANIES WERE REQUIRED TO, AND DID, PASS ON THE FULL AMOUNT OF THE OVERCHARGES TO THE CONSUMERS.

This case presents a fundamental question: is the direct-purchaser limitation of *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), completely without exception? Petitioners suggest that unless the Court reverses the judgment below, the answer to this question, for all practical purposes, is "yes." If the Tenth Circuit's result stands, the direct-purchaser rule will be extended to an irrational point where the logical plaintiffs – those who bore *all* antitrust overcharges – will have their claims dismissed.

Section 4 of the Clayton Act, 15 U.S.C. § 15, permits "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws" to maintain an action to recover treble damages. Despite this seemingly clear language, the Court in *Illinois Brick* decided on policy grounds generally to limit antitrust standing under Section 4 to direct purchasers, and to preclude suits by persons more remote in the distribution chain. Even though indirect purchasers might also suffer some injury, the Court reasoned, problems of proof, considerations of antitrust enforcement, and the risk of multiple recoveries all argued for a general rule allowing only direct purchasers to sue.

The Court in *Illinois Brick* also recognized, however, as it had earlier in *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968), that there might be cases where it would be unwise to limit antitrust recoveries only to direct purchasers. This is such a case. Here the utilities' tariffs *required* them to pass on the entire overcharge to their residential consumers, and the utilities did so. The attorneys general have now brought suit on behalf of their residential consumers to recover the overcharges that they, and they alone, sustained. It would turn *Illinois Brick* on its head to hold that under these circumstances the injured consumers must give way as plaintiffs to utilities that absorbed none of the overcharges.

A. The Complete Pass-On Of Overcharges In A Regulated Cost-Plus Setting Satisfies All The Court's Concerns In *Illinois Brick*.

The rationale for the *Illinois Brick* direct-purchaser rule does not exist in this case. Here the indirect

purchasers – the residential consumers – are the parties who bore the overcharge. The amount of that overcharge is easily shown from utility company filings. This suit will not be made appreciably more complicated by recognizing the consumers' claims. The utilities cannot simultaneously enforce the antitrust laws and ensure compensation to injured parties. The consumers can. Antitrust enforcement will be enhanced, not hindered, if the persons actually suffering injury are allowed to maintain this suit.

1. Overcharges Directly Passed On To Customers Of Regulated Utilities Are Easy To Prove.

This Court's primary concern in *Illinois Brick* was the potential for complicating, and ultimately frustrating, antitrust enforcement if all persons who conceivably suffer injury were allowed to sue in a given case. The Court suggested that allowing all indirect purchasers to sue might turn antitrust suits into large-scale battles over apportionment of damages:

> Permitting the use of pass-on theories under § 4 essentially would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge – from direct purchasers to middlemen to ultimate consumers. However appealing this attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness.

431 U.S. at 737.

The Court recently emphasized this desire for uncomplicated litigation in *California v. ARC America Corp.*, ___ U.S. ___, 109 S.Ct. 1661, 1666 n.6 (1989):

> In Illinois Brick, the Court was concerned not merely that direct purchasers have sufficient incentive to bring suit under the antitrust laws, as the Court of Appeals asserted, but rather that at least some party have sufficient incentive to bring suit. Indeed, we implicitly recognized as much in noting *that indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them.*

(Citation omitted) (emphasis added).

This case satisfies the Court's basic concern. It is easy for the residential consumers here to prove that the entire overcharge was passed on to them. These consumers, represented *parens patriae* by their attorneys general, have demonstrated ample incentive to sue.

There is no question that the plaintiff utility companies simply transferred the entire overcharge to their customers. In the words of KPL Vice-President and General Counsel David S. Black:

> Essentially we [KPL] provide a transportation service, and have title to the gas for the few hours required to move it from the wellhead to the burner tip. As the cost of this gas changes, it is reflected in our customers' bills, through the operation of the purchased gas adjustment mechanism, penny for penny and dollar for dollar.[7]

[7] Ex. D to Doc. No. 485, pp. 2-3. The regulatory mechanism operates the same way with respect to respondent UtiliCorp.

The injury was sustained by the utilities' customers, not the utilities themselves. As Mr. Black noted, the consumers "pay *all* of any increases in the cost of natural gas KPL must purchase to serve them." *Id.* at 1-2 (emphasis original).[8]

Therefore, unlike the situation in *Hanover Shoe* and *Illinois Brick*, there is no problem here in determining how the utilities set their prices. The present case has mandatory cost-plus pricing set out in public filings. Those filings clearly show the volume and price of gas sold to residential consumers. *See* Exhibit K to Doc. No. 485. The amount of damage incurred by residential consumers is easily shown by simply multiplying the aggregate overcharge by the percentage of gas sold to those consumers.[9] This simple system reveals the direct pass-through of all overcharges. That pass-through is easy to prove: one need look no further than the utilities' public filings.

The fact that the utilities may have lost sales should not bar the residential consumers' claims. The consumers have no interest in, or claim to, the utilities' lost profits.[10]

[8] For purposes of its decision, the Tenth Circuit assumed what was in fact the case – a 100% pass-through of overcharges. Pet. App. A14. Thus, the concern expressed by the United States in its *amicus* brief in support of the States' petition for writ of certiorari – that complexity may result if parties are allowed to litigate the extent of any pass-on – does not apply in this case.

[9] This type of "aggregate" damages proof is specifically authorized in a *parens patriae* case by 15 U.S.C. § 15d.

[10] The United States, in its *amicus* brief in support of the States' petition for writ of certiorari, questioned whether allowing both direct and indirect purchasers to pursue their

(Continued on following page)

The unreasonably complex proof that the Court confronted in *Illinois Brick* would arise only if the residential consumers and the utilities were seeking apportionment of the *same* damages – the overcharges. But in the present case, where the overcharges were passed on in their entirety, this problem does not exist. The attorneys general can pursue the damages that the consumers alone sustained, and the utilities can seek their lost profits. With no overlap of damages, there is no problem of apportionment.

For the same reasons, there is no risk here of the duplicative recoveries that the Court feared in *Illinois Brick*. Here both the direct and indirect purchasers are present in the same suit. Under the approach outlined by petitioners, all will remain as plaintiffs – the utilities to recover their lost sales, and the consumers to recover the overcharges they paid. The different classes of plaintiffs will be seeking different – not duplicative – damages.[11]

(Continued from previous page)

respective damage claims could present difficulty regarding "whether lost sales are attributable to higher charges or some other factor." These issues, however, are part of *every* case where lost profits are alleged; no additional complexity is introduced by allowing indirect purchasers to pursue the claims for overcharges.

[11] Moreover, unlike *Illinois Brick*, where allegedly price-fixed concrete blocks were incorporated into buildings after passing through several levels of distribution, here a single product, natural gas, passed unchanged from the producers to the ultimate consumers. The *Illinois Brick* facts required a complex economic analysis of how much the price of concrete block affected the ultimate price of the buildings. In the present case, of course, no such analysis is necessary.

These precise points were made by the *en banc* Seventh Circuit in *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.), *cert. denied*, 109 S.Ct. 543 (1988). In an opinion written by Judge Richard Posner, the Seventh Circuit addressed the identical issue presented here: whether a 100% pass-through of overcharges by a regulated utility should be recognized as an exception to the *Illinois Brick* direct-purchaser rule. In holding that it should, the Seventh Circuit disposed of the argument that allowing indirect purchasers to sue would appreciably increase the suit's complexity:

> Thus there can be no problem of apportionment in the suit on behalf of the residential customers. Those customers are not seeking damages for gas they did not buy, and the damages for the gas they did buy can simply be read off from their gas bills.
>
> * * *
>
> Since [the utility] can sue for its lost sales . . . , there can be more than one set of plaintiffs. But each set will be suing in respect of different sales – not, as in *Illinois Brick*, the same sales.

852 F.2d at 897.

Judge Posner's analysis applies equally to the present facts. Here too the consumers' damages can be determined from their gas bills, or, even more simply, from the utilities' public filings. The Court's concerns in *Illinois Brick* do not arise.

This case does not require the application of complex economic theory. Nor does it rest on dubious assumptions about hypothetical pricing decisions. The indirect purchasers' claims should be restored.

2. Recognizing The Residential Consumers' Claims Will Promote Antitrust Enforcement And Ensure Compensation For Those Parties Actually Injured.

The Court in *Illinois Brick* had two additional concerns: encouraging antitrust enforcement and ensuring that injured parties receive compensation. Unlike *Illinois Brick*, in the present case both interests can be furthered only by allowing the *indirect* rather than the direct purchasers to sue for the antitrust overcharges.

The state attorneys general, as representatives of the consumers actually sustaining damages, are the most reliable parties to pursue the overcharges on the present facts. The utilities clearly are not. Of the fifty regulated gas utilities in the relevant service areas in Kansas and Missouri, only *two* – KPL and UtiliCorp – chose to bring suit here. UtiliCorp dismissed its complaint in 1986, less than a year after filing suit. Although UtiliCorp later refiled, defendants maintain that UtiliCorp's claims (and thus, if the direct-purchaser rule is applied, the claims of more than 40,000 customers) are time-barred. The failure of the remaining forty-eight utilities to bring suit *at all* means that currently at least 50,000 *more* residential consumers are unrepresented and will remain so if the *parens patriae* claims are not allowed to proceed.

The Seventh Circuit in *Panhandle Eastern* recognized that in the regulated utility industry, the utilities, unlike most direct purchasers, have little incentive to sue. As the court noted:

> The public utility has less to gain from suit than the direct purchaser in the case of the purely

> private contract. The public utility commission may force the utility to pass on to the consumers any and all damages that the utility recovers, and if it does utilities will have no incentive to sue because they will have nothing to gain from suit.
>
> * * *
>
> [The utility] seems a most reluctant suitor, and why shouldn't it be? It has little or nothing to gain by such a suit.

852 F.2d at 895.

On balance, the utilities operating in Kansas and Missouri also seem reluctant to sue. Even KPL, the only utility plaintiff that did sue promptly, cannot be said to have sufficient incentive to continue prosecuting this case vigorously.[12] The Tent , Circuit suggested that KPL might ultimately be required by regulators to pass on any recovered overcharges to its customers. Pet. App. A11. If so, what incentive does it have to pursue these claims forcefully to a conclusion? How long can KPL's efforts to obtain damages on behalf of others be reconciled with its obligations to its own shareholders?

If, on the other hand, KPL is attempting to keep all overcharges for itself, it would have incentive to sue, but any overcharge it recovered would be a complete windfall. The Court's announced goal in *Illinois Brick* of providing compensation to injured parties would be wholly

[12] KPL's motivation is questionable in part because of its need to maintain good relationships with the very suppliers it has sued. *See Illinois Brick*, 431 U.S. at 746.

frustrated.[13] Allowing the utilities that absorbed *none* of the overcharge to sue, while denying this same right to the consumers who sustained *all* of it, does nothing to promote compensation. The *Illinois Brick* direct-purchaser rule, which has never been more than an exception to the general rule of antitrust standing, cannot sensibly be extended here to deprive the only truly-injured parties of their claims.

The position advanced by the States is consistent with the flexible, common-sense approach adopted by the Court in *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982). There plaintiff was a subscriber, through her employer, to a health plan that denied her claim. Despite the fact that plaintiff was only an indirect purchaser of the health plan's services, she was allowed to maintain an antitrust suit against the plan. In holding that the direct-purchaser rule of *Illinois Brick* did not apply, the Court recognized that "it is not the employer as purchaser, but its employees as subscribers, who are out of pocket as a consequence of the plan's failure to pay benefits." 457 U.S. at 475. The Court recognized that under these circumstances:

> [O]ur cautious approach to speculative, abstract or impractical damages theories has no application. . . .The nature of [plaintiff's] injury is easily

[13] This is not a case such as *Illinois Brick*, where a great number of potential plaintiffs, including the direct purchasers themselves, absorbed part of the overcharge. While in the *Illinois Brick* setting, allowing only direct purchasers to sue clearly compensates *some* injured parties, and arguably leaves uncompensated only the more remote purchasers, allowing the utilities to sue in the present case would not compensate *any* party who bore the overcharges.

> stated: As the result of an unlawful boycott, Blue Shield failed to pay the cost she incurred for the services of a psychologist. Her damages were fixed by the plan contract and, as the Court of Appeals observed, they could be "ascertained to the penny."

Id. at 475 n.11.

The present case is no different. It is the residential consumers who have suffered "tangible economic injury," *id.*, and it is they who should be allowed to sue.

The Court also suggested in *Illinois Brick* that the potentially small stake of indirect purchasers may impede antitrust enforcement if they are granted standing to sue. But the *parens patriae* mechanism of 15 U.S.C. § 15c is designed to remedy that exact concern. *See* H.R. No. 94-499, 94th Cong., 2d Sess. 6-8, *reprinted in* 1976 U.S. Code Cong. & Ad. News 2572, 2575-78. Certainly the huge aggregate claim of residential consumers in this case has given the attorneys general ample incentive to sue. *See* 15 U.S.C. § 15d.

The goals of antitrust enforcement and compensation to injured parties can only be achieved by allowing the *parens patriae* claims to proceed.

B. The Regulated Cost-Plus Pricing Arrangement In This Case Satisfies The Exception To The Direct-Purchaser Rule Suggested By The Court In *Hanover Shoe, Illinois Brick* And *ARC America*.

Not only does the present case satisfy the underlying concerns of *Illinois Brick*, it also fits within the cost-plus

exception suggested in *Hanover Shoe, Illinois Brick* and *ARC America*.

In *Hanover Shoe*, the Court noted that "there might be" an exception to the direct-purchaser rule, "for instance, where an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." 392 U.S. at 494. In *Illinois Brick*, the Court elaborated on what it termed the *Hanover Shoe* "example" of a "pre-existing cost-plus contract":

> In such a situation the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price. The effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand that complicates the determination in the general case. The competitive bidding process by which the concrete block involved in this case was incorporated into masonry structures and then into entire buildings can hardly be said to circumvent complex market interactions as would a cost-plus contract.

431 U.S. 735-36.

In *ARC America*, the most recent case in which the Court discussed this issue, it again noted that "indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them." 109 S.Ct. at 1666 n.6.

The Court's primary concern in these cases appears to have been avoiding complex problems of proof. Preexisting cost-plus contracts may avoid these problems, as the Court noted. So do the facts here, where the indirect

purchasers paid the entire overcharge under a classic pre-existing, cost-plus arrangement. If this case does not satisfy the exception to the direct purchaser rule, it is doubtful that any would.

As the Seventh Circuit reasoned in *Panhandle Eastern*, this Court cannot have intended to prescribe a mechanical "fixed-quantity" test for determining whether to allow indirect purchaser suits.[14] The importance of a fixed-quantity contract is to ensure that the direct purchaser has passed on the entire overcharge rather than absorbing part of it to avoid losing customers. *Panhandle Eastern*, 852 F.2d at 895. No fixed-quantity contract is necessary in the present case because the entire overcharge *was* passed on to the consumers. The utilities were required by their tariffs to pass on the full overcharge, and they did so.[15]

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[14] The Tenth Circuit assumed that a contract for a "fixed-quantity" is essential to any exception to the direct-purchaser rule, erroneously believing that problems of apportionment would otherwise exist between the utilities' lost profits and the consumers' overcharges. But these are wholly separate elements of damage that do not need to be "apportioned." *Panhandle Eastern*, 852 F.2d at 897. In this case, as in *Panhandle Eastern*, there is no need to engage in the complex task of trying to apportion the *same* damages between the utilities and the consumers.

[15] This result is consistent with economic theory. As Judge Posner noted, in the context of regulated public utilities, where prices charged consumers are generally lower than they would be in the absence of regulation, and where residential consumers have no ready alternative source of fuel, one would expect an economically rational utility to pass on the full amount of the overcharge. 852 F.2d at 896. "The utility can force the whole of the cost increase through to its residential customers without sacrificing any profits, *and did so*." *Id.* at 898 (emphasis original).

The hypothetical result that this Court expected to occur under the "pre-existing cost-plus" contract of *Hanover Shoe* and *Illinois Brick* – a 100% pass-through of incurred overcharges – already exists on the present facts. There is no ground for denying the injured consumers their right to sue.

II. THE INDIRECT PURCHASERS' CLAIMS SHOULD BE RECOGNIZED HERE FOR THE SEPARATE REASON THAT, UNLIKE *ILLINOIS BRICK*, THIS CASE IS BROUGHT BY STATE ATTORNEYS GENERAL AS *PARENS PATRIAE*

The Court should reverse the Tenth Circuit's judgment for the separate reason that the States' *parens patriae* actions are authorized by Title III of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 15c (the "Act"). The language and legislative history of the Act make plain that state attorneys general have standing to bring antitrust suits on behalf of "natural persons" injured by antitrust violations, regardless of whether those persons are direct or indirect purchasers.

The full extent of the *parens patriae* authority conferred by the Hart-Scott-Rodino Act has never been addressed by the Court. In *Illinois Brick*, the Court rejected the argument that the Act evinces a congressional intent to authorize *all* suits brought by indirect purchasers under Section 4 of the Clayton Act, 15 U.S.C. § 15.[16] 431 U.S. at 733 n.14; *but see* 431 U.S. at 756-58 (Brennan, J.,

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[16] The Court suggested that legislators' views in 1976 cannot possibly have affected general standing principles under Section 4 of the Clayton Act, which was enacted in 1914. 431 U.S. at 733 n.14.

dissenting). But *Illinois Brick* was not a *parens patriae* case.[17] It therefore did not directly address the issue now before the Court: whether the Act grants independent authority to state attorneys general to bring suit in their *parens patriae* capacity on behalf of indirect purchasers.

Title III, Section 301 of the Hart-Scott-Rodino Act, 15 U.S.C. § 15c(a)(1), provides in pertinent part:

> Any attorney general of a State may bring a civil action in the name of such State as parens patriae on behalf of natural persons residing in such State . . . to secure monetary relief as provided in this section for injury sustained by such natural persons to their property by reason of any violation of the Sections 1 to 7 of this title.

The plain language of the Act thus authorizes the precise action brought in this case.

The Act cannot sensibly be read as authorizing *parens patriae* actions only on behalf of direct purchasers. The clear purpose of the Act is to protect *consumers*,[18] who are far more likely to be *indirect* rather than direct purchasers. *See* Kintner, Griffin & Goldston, *The Hart-Scott-Rodino Antitrust Improvements Act of 1976: An Analysis*, 46

[17] In *Illinois Brick*, the State of Illinois was suing for itself and its political subdivisions, not in a *parens patriae* capacity. The observations of the *Illinois Brick* majority regarding the Act were thus not directed at suits brought under 15 U.S.C. § 15c, but at indirect purchaser suits brought under Section 4 of the Clayton Act, 15 U.S.C. § 15.

[18] The Act's legislative history confirms that its purpose is to allow "State attorneys general to act as *consumer* advocates in the enforcement process. . . ." *See* H.R. No. 94-499, 94th Cong., 2d Sess. 8, *reprinted in* 1976 U.S. Code Cong. & Ad. News 2572, 2578 (emphasis added).

Geo. Wash. L. Rev. 1, 23 (1977). The Court has recognized that protecting consumers was a central goal of the Act. In *Reiter v. Sonotone Corp.*, 442 U.S. 330, 344 n.7 (1979), the Court expressly noted that "[t]he text and legislative history of this statute make clear that in 1976 Congress believed that consumers have a cause of action under § 4, which the statute authorizes the states to assert in a parens patriae capacity."

When debating the Act, Congress recognized that in order to adequately protect consumers from antitrust violators, the "technical and procedural" barriers erected by such concepts as "standing" and "privity" would have to be rejected:

> "A direct cause of action is granted the States to avoid the inequities and inconsistencies of restrictive judicial interpretations. . . . Section 4C is intended to assure that consumers are not precluded from the opportunity of proving the amount of their damage and to avoid problems with respect to manageability [of class actions], *standing, privity, target area, remoteness, and the like.*"

Illinois Brick, 431 U.S. 720, 757 (Brennan, J., dissenting) (quoting S. Rep. No. 94-803, 94th Cong., 2d Sess. 42 (1976) (emphasis supplied by Court)).

As Justice Brennan further noted, Representative Rodino, one of the Act's sponsors, stated during the House debates:

> "[A]ssuming the State attorney general proves a violation, and proves that an overcharge was 'passed on' to the consumers, injuring them 'in their property'; that is, their pocketbooks – recoveries are authorized by the compromise bill

> *whether or not the consumers purchased directly from the price fixer, or indirectly, from intermediaries, retailers, or middlemen.* The technical and procedural argument that consumers have no 'standing' whenever they are not 'in privity' with the price fixer, and have not purchased directly from him, is rejected by the compromise bill. Opinions relying on this procedural technicality . . . are squarely rejected by the compromise bill."

Id. at 757-58 (quoting 122 Cong. Rec. H10295 (daily ed. Sept. 16, 1976)) (emphasis added).

These statements make plain that Congress intended to authorize state attorneys general to sue as *parens patriae* on behalf of indirect purchaser consumers. "It is difficult to see how Congress could have expressed itself more clearly." 431 U.S. at 758 (Brennan, J., dissenting). While the passage of the Act may not have affected antitrust standing generally, surely Congress intended to – and did – authorize *parens patriae* actions on behalf of indirect purchasers.[19]

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[19] The majority in *Illinois Brick* found it significant that some members of Congress apparently believed the *parens patriae* provisions "create no new substantive liability." *See* 431 U.S. at 733 n.14. But such statements should have no bearing on the right of state attorneys general to sue on behalf of indirect purchasers. When these statements were made in 1976, Congress clearly thought that indirect purchaser suits *could* be brought. H.R. 94-499 at 6 n.4; *see also Illinois Brick*, 431 U.S. at 733 n.14. Because the Act was based on the assumption that indirect purchaser suits were allowed, "Congress need not have intended to create a new remedy, since one already existed." *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 378 (1982).

Application of the *Illinois Brick* direct-purchaser rule would undermine the clear language and legislative history of the Act. As Congress recognized, claims of consumers against manufacturers or distributors are by their very nature indirect. The *parens patriae* claims here were specifically authorized by Congress in 1976. Those claims should be reinstated.

CONCLUSION

The judgment of the Tenth Circuit should be reversed and the *parens patriae* claims of the state attorneys general should be allowed to proceed.

Respectfully submitted,

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No. 88-2109

In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI,
AS PARENS PATRIAE,

Petitioners,

v.

UTILICORP UNITED INC.,

Respondent.

On Writ Of Certiorari To The United States
Court Of Appeals For The Tenth Circuit

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QUESTION PRESENTED

Petitioners' "Questions Presented" violate Supreme Court Rule 21.1(a) by the presentation of argumentative and repetitious questions. The issue presented to this Court should be the question certified by the District Court for interlocutory appellate review and ruled by the United States Court of Appeals for the Tenth Circuit pursuant to 28 U.S.C. § 1292(b):

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

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No. 88-2109

In The

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THE STATES OF KANSAS AND MISSOURI, AS PARENS PATRIAE,

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On Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

BRIEF FOR RESPONDENT UTILICORP UNITED INC.

STATUTE INVOLVED IN THE CASE

In their petition for a writ of certiorari, the States of Missouri and Kansas cited the Court to Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982). In their brief on the merits, petitioners also seek to rely substantively on portions of Title III of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. §§ 15c, 15d, and 15e. The States did not rely substantively on Sections 4c through 4e in the Courts below.

STATEMENT OF THE CASE

A. Background.

UtiliCorp United Inc. sells natural gas to industrial, commercial, and residential customers in 12 towns in western Missouri through its Missouri Public Service division ("MPS") and in Lawrence, Kansas, through its Kansas Public Service division ("KPS"). J.A. 5, Doc. No. 440 at 61.[1] During the time of the anticompetitive combination alleged in its Complaint, UtiliCorp purchased natural gas directly from Williams Natural Gas Company ("Pipeline"). *Id.* at 7.

Pipeline had purchased that natural gas from various suppliers, including Amoco Production Company ("Amoco"), Cities Service Oil & Gas Corporation ("Cities Service"), CSG Exploration Company ("Exploration"), the Moxa Limited Partnership ("Moxa"), and the Wamsutter Limited Partnership ("Wamsutter"). *See id.* at 9, 12-13.

In September 1984, The Kansas Power and Light Company ("KPL") filed a Complaint in Missouri pursuant to Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982), against defendants Pipeline, Amoco, Cities Service, Exploration, Moxa, and Wamsutter. Doc. No. 2. UtiliCorp subsequently intervened and filed a substantially similar Complaint against the same defendants alleging, *inter alia*, that the defendants, acting in combination, artificially inflated and fixed the price of natural gas that was produced by them in Wyoming and

[1] References to "Doc. No. ___" are to the list of relevant docket entries in the Joint Appendix.

sold in interstate commerce by Pipeline to UtiliCorp and other direct natural gas purchasers. Doc. Nos. 60, 378.[2] The utilities' case was transferred to Oklahoma and ultimately to Kansas.

UtiliCorp seeks to recover overcharge damages for all natural gas purchased directly from the defendants which it used in its own operations or resold to its residential, industrial, and commercial customers. *See* Doc. No. 440 at 13-14. UtiliCorp also seeks to recover from defendants the margin[3] it lost as a result of decreased sales of natural gas due to defendants' anticompetitive conduct. *Id.*

Defendants asserted as an affirmative defense to UtiliCorp's Complaint that UtiliCorp had passed on any illegal overcharges to its customers ("the pass-on defense"). *Id.* at 2-3 and n.1. Defendants claimed that UtiliCorp therefore lacked standing under Section 4 of the Clayton Act and had not been injured within the meaning of that statute. *Id.* at 3.

[2] Although it is not included in the Joint Appendix, UtiliCorp's First Amended Complaint was filed on August 3, 1989. The latest amendments have no bearing on the issues before this Court.

[3] In their Brief, petitioners simplistically refer to the utilities' lost profit claims. *See, e.g.*, Petitioners' Brief at 14-15. In fact, the utilities' damage claims encompass both a rate of return element that was lost due to defendants' conduct and an amount representing the portion of the utilities' fixed costs which they were not able to recover because of defendants' conduct. The utilities' damage calculations are more complicated than the States' Brief would suggest.

Following the utilities' lead, the States of Kansas and Missouri filed Complaints under Section 4 of the Clayton Act against the same defendants in July of 1985 and August of 1986, respectively. J.A. 1. The States' allegations are virtually identical to those of the utilities. *Id.* The petitioners seek to recover overcharge damages on behalf of state agencies and municipalities[4] that purchased natural gas directly or indirectly from Pipeline and as *parens patriae* on behalf of indirect residential gas customers in their respective states. Doc. Nos. 345, 348.

The States do not – and cannot – assert claims on behalf of UtiliCorp's industrial and commercial natural gas customers in Kansas and Missouri. As a result, the States' *parens patriae* claims represent no more than 50 percent of the natural gas sold by the Pipeline in Missouri and Kansas. Exhibit A to Doc. No. 440 at 2, ¶ 4; Exhibit B to Doc. No. 440 at 2, ¶ 3. Acceptance of the States' *parens patriae* claims and the defendants' corresponding pass-on defenses would eliminate more than 50 percent of the antitrust damages asserted by the utilities in this case against the defendant producers and suppliers. *Id.*

B. Proceedings Below.

In December 1987, UtiliCorp filed a motion to strike or for partial summary judgment on those affirmative

[4] The States' claims on behalf of direct purchaser cities which distribute natural gas to their residents through a municipal utility are analogous to the claims of UtiliCorp. For example, the City of Springfield, Missouri, has claims for all overcharges, including those it passed along to residential, industrial, and commercial customers, in an amount exceeding UtiliCorp's overcharge damages. *See* Doc. No. 348.

defenses asserted by Amoco, Cities Service, and Pipeline which were based on the pass-on theory rejected in *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968). Doc. No. 440. Shortly thereafter, KPL filed a similar motion. Doc. Nos. 448, 449.

Contrary to the States' representation at page 6 of Petitioners' Brief, neither UtiliCorp nor KPL asked for dismissal of the States' *parens patriae* claims – the motions were directed solely toward defendants' affirmative defenses. *See* Doc. No. 440. The private counsel hired to represent Missouri and Kansas insisted that the District Court also consider the dispute as a motion to dismiss the States' *parens Patriae* claims. *See* Doc. Nos. 474, 485.

The District Court, the Honorable Dale E. Saffels,[5] found on uncontested evidence that UtiliCorp and KPL did not resell natural gas pursuant to cost-plus contracts for fixed quantities. *In re Wyoming Tight Sands Antitrust Cases*, 695 F. Supp. 1109 (D. Kan. 1988), *aff'd*, 866 F.2d 1286 (10th Cir. 1989), *cert. granted sub nom. Kansas v. Kansas Power & Light Co*, 110 S. Ct. 833 (1990)(A34). Accordingly, it entered partial summary judgment prohibiting the defendants from asserting pass-on defenses to the antitrust claims of UtiliCorp and KPL. *Id.*

Following the suggestion of the States' counsel that issues of the States' *parens patriae* standing and injury also

[5] Prior to his appointment to the federal bench, Judge Saffels had extensive experience in utility regulation. He served as a member and then as Chairman of the Kansas Corporation Commission, which regulates Kansas utilities, from 1967 to 1975.

be resolved, the District Court dismissed the States' *parens patriae* claims pursuant to the holding of *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), prohibiting offensive use of pass-on theories. In so ruling, the District Court made no determination regarding the amount of illegal overcharges allegedly passed on by UtiliCorp to its customers. *Wyoming Tight Sands*, A33-34.

In neither the District Court nor in the Court of Appeals for the Tenth Circuit did counsel for the States contend that Section 4c of the Clayton Act created an independent cause of action for state attorneys general on behalf of indirect purchasers. *See* Doc. Nos. 474, 485. The District Court did not address that issue, which was briefed for the first time in this Court in petitioners' brief on the merits.

None of the defendants appealed from the District Court's entry of partial summary judgment prohibiting their use of pass-on defenses. On the States' motion, the District Court certified for interlocutory appeal the question of whether indirect residential purchasers of natural gas may join their own local distribution companies in asserting federal antitrust claims against the producers and an intermediary pipeline supplier of natural gas. Doc. Nos. 528, 541. The Court of Appeals for the Tenth Circuit granted the States' unopposed petition for permission to appeal. Doc. No. 555.

The Court of Appeals affirmed Judge Saffels' Order, concluding that the rulings and rationales underlying *Hanover Shoe* and *Illinois Brick* prohibit the needless and expensive complication of ongoing federal antitrust litigation which the States' *parens patriae* claims would

cause. *Wyoming Tight Sands*, A17. Although the Court below recognized that the States had not argued that Section 4c of the Clayton Act eliminates the *Illinois Brick* direct purchaser rule, it assumed that under Section 4c, citizens of a state must have standing in order for the state attorney general to sue in its *parens patriae* capacity. *Id.* at A7 n.1. The Court of Appeals implicitly concluded that the utilities' residential customers are indirect purchasers barred from recovery by *Illinois Brick*.

Petitioners' Statement of the Case ends with one misleading statement that demands correction: the suggestion that "the utilities will be entitled to recover *for their own benefit* all of the antitrust overcharges. . . ." Petitioners' Brief at 8 (emphasis added). The utilities have always acknowledged that recovery of overcharges will be passed back to the customers. *See, e.g.*, Doc. No. 440 at 17-18 ("UtiliCorp recognizes that its consumers will be the ultimate beneficiaries of much of the recovery extracted from defendants as damages.").

As Judge Saffels found, "[i]f the utilities prevail on their antitrust claim, their recovery will be passed on to the consumers either through a reduction in prices or through a rebate. This appears to be an eminently fair and efficient means of apportioning any damage award, much more so than through protracted litigation." *Wyoming Tight Sands*, A36. Despite this knowledge, the utilities have pursued this litigation vigorously, at no cost to the ratepayers, to protect their markets, recover their lost margins, and win a treble damage award.

SUMMARY OF THE ARGUMENT

This case presents a straightforward issue of antitrust policy: Should this Court continue to consolidate antitrust damage claims in the hands of an injured direct purchaser to reduce complexities and maximize the incentive to sue? Or, instead, should the Court cloud the clear rule of *Hanover Shoe* and *Illinois Brick* with a regulated utility exception created for the benefit of state attorneys general suing in their *parens patriae* capacity on behalf of some customers who ultimately paid some of the overcharges?

UtiliCorp is clearly an injured direct purchaser under Section 4c of the Clayton Act and this Court's precedents. As a direct purchaser of gas from an anticompetitive combination, UtiliCorp suffered more than $4 million in lost margin damages which were not "passed on" to its customers, and it paid more than $12 million in overcharges. While most of the overcharges were passed on to residential, commercial, and industrial customers, the States' claim that residential customers in Kansas and Missouri "bore *all* antitrust overcharges," Petitioners' Brief at 10 (emphasis added), is false.

In this case, the utilities are in the best position to maintain antitrust claims. They have ample incentive to pursue millions of dollars in damages and can also satisfy the concerns of the state public service commissions by passing through much of the recovery to their customers. Concentrating the claims in the utilities avoids complex battles over apportionment of damages and the disincentive of fragmenting the recovery among multiple levels of purchasers.

To the extent that the Court in *Illinois Brick* hypothesized an exception to the direct purchaser rule for fixed quantity, cost-plus contracts, that theoretical exception does not apply to this case because UtiliCorp never sold gas pursuant to fixed quantity contracts. The States' *parens patriae* claims do not "fit squarely within the 'cost-plus' exception," Petitioners' Brief at 8.

Petitioners' attempt to claim that Section 4c of the Clayton Act creates an independent cause of action cannot be considered by this Court because it was never raised below. Moreover, in *Illinois Brick* this Court rejected the notion that the Hart-Scott-Rodino Antitrust Improvements Act of 1976 created a new remedy for indirect purchasers represented by state attorneys general. Subsequent testimony by state attorneys general and comments by members of Congress confirm that this Court's interpretation was and is correct. On several occasions, Congress has refused to amend Section 4c to repeal or modify the *Illinois Brick* direct purchaser rule, thus demonstrating Congress' approval of the case and the rule it announced.

ARGUMENT

I. UTILICORP'S SECTION 4 CLAIMS ARE PROPER BECAUSE IT SUSTAINED ANTITRUST INJURIES INFLICTED BY THE DEFENDANTS.

More than 20 years ago, this Court identified the direct purchaser as the proper plaintiff to pursue damages resulting from antitrust violations under § 4 of the Clayton Act. *See Hanover Shoe*. The Court reached that

conclusion even though it recognized that the direct purchaser could have passed on all illegal overcharges to its customers. *Hanover Shoe*, 392 U.S. at 489-91 and n.8.

UtiliCorp is a direct purchaser of natural gas from the defendant combination. As a result of the defendants' anticompetitive conduct, UtiliCorp has sustained antitrust injury in excess of $4 million in lost margin damages. In addition, it paid more than $12 million of overcharges for natural gas from the defendants' combination.

Roughly half of that gas was resold to the residential customers the Attorneys General attempt to represent. *See* Exhibit A to Doc. No. 440 at 2, ¶ 4; Exhibit B to Doc. No. 440 at 2, ¶ 3. Most of the rest[6] was sold to industrial and commercial customers who are not represented in the *Wyoming Tight Sands* litigation. *Id.*

Even though UtiliCorp was ultimately reimbursed for most of the overcharges when its customers purchased the gas, under Section 4(a) of the Clayton Act UtiliCorp is the proper party to seek recovery for both the overcharges and the lost margin damages it suffered. *See Hanover Shoe*, 392 U.S. at 489.

[6] UtiliCorp also uses small amounts of Pipeline gas for internal operations, principally for heating company facilities and to power turbine peaking units in MPS' electrical distribution network.

In 1977, this Court reaffirmed the policies and principles of *Hanover Shoe* in *Illinois Brick*. In that case, the Court refused to allow an indirect purchaser to claim antitrust injury. Once again, a direct purchaser's ability to pass on overcharges to its customers did not create injury and standing under federal antitrust laws on the part of the indirect purchasers who absorbed the overcharges.

This Court invited parties dissatisfied with that rule to seek legislative amendments to the Court's interpretation. *Illinois Brick*, 431 U.S. at 733-34 n.14. Congress has rejected every proposal to effect such changes.

Having failed in their efforts to overrule *Illinois Brick* legislatively, the state attorneys general are back before this Court, seeking to whittle away at the basic federal antitrust principle that direct purchasers suffer the antitrust injury. Yet in the thirteen years since *Illinois Brick* was decided, nothing has occurred to justify a judicial exception to the rule that direct purchasers who suffer some damage incur an injury to their business or property as contemplated in Section 4 of the Clayton Act.

In *ARC America*, this Court recently reaffirmed the direct purchaser rule, stating flatly that "[a]s construed in *Illinois Brick*, § 4 of the Clayton Act authorizes only direct purchasers to recover monopoly overcharges under federal law." *California v. ARC America Corp.*, 490 U.S. ___, 109 S. Ct. 1661, 1666, 104 L. Ed. 2d 86, 96 (1989). The policies underlying this rule support the Court of Appeals' judgment in this case.[7]

[7] The States have cited a footnote from *ARC America* out of context in an attempt to carve greater territory for indirect

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II. FEDERAL ANTITRUST POLICY SUPPORTS CONCENTRATING DAMAGES IN THE HANDS OF THE DIRECT PURCHASER TO INCREASE HIS INCENTIVE TO ACT AS A PRIVATE ATTORNEY GENERAL.

The issue of antitrust policy before the Court is whether it remains wise to consolidate antitrust damage claims in the direct purchaser in order to maximize the incentive for private parties to sue. Effective enforcement of the antitrust laws depends on the vigor of private attorneys general in pursuing treble damage awards for their own profit. Deterrence is furthered more by concentrating a claim in the hands of a direct purchaser utility with a large damage claim and a profit motive than by splitting off parts of that claim to be handled by the overworked staffs of various state attorneys general.

The States search for an exception to the direct purchaser rule of *Hanover Shoe* and *Illinois Brick* based on an

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purchasers than permitted by *Hanover Shoe* or *Illinois Brick*. *See* Petitioners' Brief at 13. The Court's primary concern in footnote 6 to *ARC America* was not to diminish the injury or standing of direct purchasers such as UtiliCorp, but to ensure that "at least some party have sufficient incentive to bring suit." *ARC America*, 109 S. Ct. at 1666 n.6, 104 L. Ed. 2d at 96 n.6. For the reasons set forth below, that incentive properly belongs to the utilities who purchased directly from the anticompetitive combination.

Petitioners also inaccurately characterize *Blue Shield of Virginia v. McCready*, 457 U.S. 465 (1982), as an "indirect purchaser" case. *See* Petitioners' Brief at 19-20. In *McCready*, this Court found that the plaintiff was essentially the direct purchaser. *Id.* 457 U.S. at 475.

expansive reading of hypothetical illustrations suggested in those opinions and on the Seventh Circuit's regulated utility exception posited in *Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.)(en banc), *cert. denied*, 109 S. Ct. 543 (1988). This Court's hypothetical exception to the direct purchaser rule recognized that the direct purchaser could not be damaged if it passed on 100% of the illegal overcharges *and* was insulated from declining sales and profits by a fixed quantity cost plus contract. *Hanover Shoe*, 792 U.S. at 493; *Illinois Brick*, 431 U.S. at 736.

In this case, however, the States acknowledge that the utilities can recover from the defendants lost sales and profits due to the anticompetitive combination. *See* Petitioner's Brief at 14-15. Moreover, the States conceded in their Reply Brief in the Court of Appeals that the utilities could also recover that portion of the overcharge damages attributable to the industrial and commercial customers who are not otherwise represented in this suit – a sum totalling over $100 million for UtiliCorp and KPL. States' Reply Brief at 2.[8]

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[8] The Court may note some theoretical inconsistency in the States' position on the standing/antitrust injury of indirect residential customers versus indirect industrial and commercial customers. Under Section 4c(a)(1), of course, state attorneys general cannot represent business entities. While both elected officials are pleased to represent over one million residential customers in this case, neither wants to accept responsibility for a decision of this Court that could allow the defendants to keep over $100 million of overcharge damages attributable to the industrial and commercial customers who did not bring suit.

In *Illinois Brick,* this Court recognized that "the process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid." *Illinois Brick,* 431 U.S. at 744-45. The Court further noted that "*Hanover Shoe* itself implicitly discouraged the creation of exceptions to its rule barring pass-on defenses, and we adhere to the narrow scope of exemption indicated by our decision there." *Id.* at 745.

The Court below correctly applied the principles of *Hanover Shoe* and *Illinois Brick.* In particular, the Court stressed the need to avoid the addition of unnecessary complexity and expense to this case and to ensure the efficient enforcement of federal antitrust laws. *See Wyoming Tight Sands,* A9, *citing Illinois Brick,* 431 U.S. at 737, 745-48.

First, the Tenth Circuit noted that "[c]omplex issues of proof will grow geometrically if the States press their consumers' demands" (A10), due in part to the unresolved factual issue of how much illegal overcharge was passed on to the residential consumers of each utility. Contrary to the States' promise of simple damage apportionment, the Court below recognized that "[a]ny allocation of illegal overcharges to the residential consumers may require tracing the sale from the wellhead through each level of distribution in order to establish the amount of illegal gas costs actually paid by the consumers in each state . . . " *Id.* at A12. The Tenth Circuit also correctly observed that even a perfect pass-on of all overcharges would not eliminate the need to apportion the damages

sustained by UtiliCorp as a result of decreased demand caused by defendants' inflated prices. *Id.* at A14.

A. Complexity

Because this issue was raised toward the outset of the litigation, at the beginning of deposition discovery, the parties had only rough estimates of the amount of overcharge damages, elasticities of demand, and lost margin damages that would be claimed at trial. In fact, only within the last few months have plaintiffs' economic experts completed their calculations of damages.

The complexity of such economic analyses and the time such studies take confirms this Court's preference for the simple "direct purchaser rule" of *Hanover Shoe* and *Illinois Brick.* If preliminary issues of injury and standing turned on sorting out the classes of recovery in every case, those issues would often become a procedural roadblock that defendants would use as a way to stall the litigation from proceeding on the merits. *See Associated General Contractors, Inc. v. California State Council of Carpenters,* 459 U.S. 519, 544 (1983) (in *Hanover Shoe,* the Court "noted that any attempt to ascertain damages with such precision 'would often require additional long and complicated proceedings involving massive evidence and complicated theories.' "), *quoting Hanover Shoe,* 342 U.S. at 493.

Recognizing an exception to the direct purchaser rule in this case will also greatly complicate proof of damages and could well result in jury confusion. Both risks would reduce the incentive for pursuing antitrust claims.

All these factors demonstrate why this Court should decline to adopt Judge Posner's result-oriented opinion in *Panhandle Eastern*. Even if the Court approved of the Seventh Circuit's concept, the relatively simple facts in that case do not support wide application of a new exception and distinguish it from the more complicated situation in *Wyoming Tight Sands*.

The Court in *Panhandle Eastern* dealt with the customers of a single utility in a single state with a single set of rate regulations. This case involves numerous utilities operating in four states with multiple municipal and state regulatory schemes. *See Wyoming Tight Sands*, A13-14.

The trial of this case will be complicated enough without asking the jury to apportion damages among the various parties and classes of customers they claim to represent. For example, KPL claims lost margin on all of its sales; overcharge damages attributable to all its customers in Nebraska and Oklahoma; its "own use" overcharge damages; and overcharge damages attributable to its industrial and commercial customers in Kansas and Missouri.

The States each claim overcharge damages on behalf of their residential customers and their indirect purchaser governmental customers such as universities, county governments, school districts, prisons, libraries, fire districts, and municipal governments. In addition, the direct purchaser city utilities represented by the Attorneys General are entitled to claim damages for overcharges attributable to commercial and industrial customers. Direct purchaser Farmland Industries, Inc., also claims lost profits and overcharge damages.

By the time the trial reaches UtiliCorp's separate damage claims for its Kansas Public Service and Missouri Public Service divisions as well as its "own use" and lost margin claims, the jury may be inescapably confused.

In an effort to gloss over the complexities inherent in this case, the States have failed to explain the details of natural gas distribution in Missouri and Kansas. The sale of natural gas by UtiliCorp's KPS and MPS division does not lend itself to a simple calculation of the impact of illegal overcharges by the defendants.

In attempting to describe state natural gas regulation in Kansas by the Kansas Corporation Commission ("KCC") and in Missouri (by the Missouri Public Service Commission), the States would have this Court believe that all natural gas utilities operating in Kansas and Missouri were at all relevant times subject to state authority and resold natural gas pursuant to identical state-approved Purchased Gas Adjustment ("PGA") clauses. To the contrary, the municipal utilities set their own rates. KPS, as a "one city" utility, was not subject to KCC authority until 1987 and, during most of the relevant period, did not resell natural gas by way of a PGA mechanism.[9]

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[9] In Kansas, privately-owned public utilities situated and operated wholly or principally within one city for the exclusive benefit of that city are not subject to KCC authority and regulations. *See* K.S.A. § 66-104 (1985). In 1985, UtiliCorp acquired another utility which distributes natural gas to a few Kansas towns. For this reason, the KPS division of UtiliCorp lost its "one city" exception and had to seek a KCC certificate, which was approved in November 1987.

Because KPS was not subject to KCC authority during most of the relevant period, it did not resell natural gas pursuant to a PGA mechanism. During that period, KPS presented its requests for rate adjustments to the Lawrence City Council. UtiliCorp's Motion for Partial Summary Judgment (Doc. No. 440; J.A. 5), *citing* Exhibit B, Affidavit of KPS President William A. Salome, III, at 2, ¶ 5. No formula comparable to MPS' PGA clause was used to determine or evaluate rate modifications sought by KPS. *Id.*, *citing* Salome Affidavit at 2, ¶ 6.

Although MPS is subject to Missouri Public Service Commission authority, some of the towns in which it distributes natural gas are served by another pipeline not involved in the defendant combination. This factor also complicates the damage analysis because rate cases normally covered both of the MPS gas systems.

For these reasons, UtiliCorp denies the States' unsupported contention in footnote 7 on page 13 of their Brief that the regulatory mechanism set forth in the testimony of KPL employee David S. Black "operates the same way with respect to respondent UtiliCorp." UtiliCorp's complex gas distribution systems for KPS and MPS demonstrate the wisdom of the rationales *Hanover Shoe* and *Illinois Brick*.

If the States' argument is accepted, proving or disproving plaintiffs' damages at trial will require all parties to introduce complex evidence tracking each unit of gas sold from the wellhead, through the pipeline, to the utilities, and ultimately to the burner tip. There is nothing simple or uncomplicated about the process. Asking lay

jurors to interpret damage claims based on such complicated, regulated pricing systems invites confusion and error which would be reduced greatly if UtiliCorp proves its claims directly.

B. Avoiding Multiple Liability

The risk of multiple liability which concerned the Court in *Illinois Brick*, 431 U.S. at 730, is eliminated by the Tenth Circuit's affirmance of the District Court's Order. As long as this Court maintains the direct purchaser rule of *Hanover Shoe* and *Illinois Brick*, there is no risk of multiple recovery under the federal antitrust laws.

C. Incentive

UtiliCorp claims at least $12 million in overcharge damages and $4 million in lost margin. When damages are trebled, UtiliCorp stands to recover $48 million.

Together, UtiliCorp and KPL account for roughly 75% of the overcharges and claim more than $250 million in actual damages.[10] These utilities have used their ample

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[10] Petitioners' Brief at 17 misleadingly claims that 48 Missouri and Kansas utilities failed to join this suit. All the Missouri utilities served by the Pipeline are parties to this suit: UtiliCorp, KPL, and four municipal utilities represented by the Missouri Attorney General.

In Kansas, 37 small municipal uitilities are supplied by the Pipeline. Presumably, they are all represented by the Kansas Attorney General.

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resources to mount a vigorous prosecution of the defendants' anticompetitive conduct.

The States ignore the fact that it is the utilities who, in the first instance, bear the financial responsibility for the natural gas purchased. UtiliCorp must pay for the natural gas purchased from the Pipeline, regardless of whether it ultimately recoups that amount from its customers. So long as UtiliCorp is liable as a direct purchaser for the costs of the natural gas it purchases for resale, it has more than ample incentive to monitor defendants' actions.

Moreover, UtiliCorp has an incentive to protect its markets. Industrial customers who transport gas or any customer who conserves or uses alternative fuels to reduce his purchases represents a potentially permanent loss of UtiliCorp's market. Customers who believe that the utility is looking out for their interests are more likely to defer seeking permanent alternative sources of energy.

The utilities' demonstrated commitment to the interests of their customers and the lure of treble damages has

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The only two significant Kansas utilities not represented in this lawsuit are Peoples Natural Gas and Union Gas. Those utilities have protected their customers by intervening in a proceeding pending before the Federal Energy Regulatory Commission which also challenges defendants' conduct. *See Midwest Gas Users Ass'n v. FERC*, 833 F.2d 341 (D.C. Cir. 1987).

Only a handful of tiny Kansas investor-owned utilities supplied by the Pipeline have failed to pursue either an antitrust claim or a FERC claim arising out of defendants' anticompetitive combination. Those companies' aggregate purchases total less than one percent of Pipeline's sales.

caused them to advance millions of dollars in legal fees and expenses to pursue this litigation. This hard-fought case has proceeded even though the utilities recognize that their customers will be the ultimate beneficiaries of most of the overcharge portion of any award or settlement. Nevertheless, the States continue to argue that the utilities lack incentive to sue because they passed on the overcharges. Petitioners' Brief at 18-19.

The Court of Appeals for the Tenth Circuit concluded that permitting the States to pursue their claims in this case would imperil vigorous enforcement of the antitrust laws by taking away the incentive to prosecute alleged antitrust violators from the direct purchaser – who is closer to the violator and presumably has better access to information about wrongful acts – and transferring the cost of policing and enforcing federal antitrust laws to the states. *Wyoming Tight Sands*, A14.

Rejecting the States' assertions, the Court of Appeals concluded that state attorneys general are *not* the most reliable parties to pursue overcharge damages on these facts.[11] The Court below recognized that the States'

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[11] The States' purported concern about the potential impact of the statute of limitations on UtiliCorp's antitrust claims is not well founded. A critical event which all plaintiffs describe in their Complaints was the defendants' certain amendments of gas purchase contracts on March 17, 1981. *See* Doc. No. 440 at 11-12. Both the State of Kansas and the State of Missouri filed suit more than four years after the signing of the 1981 amendments. J.A. 1. Kansas, Missouri, and UtiliCorp must all rely on arguments of fraudulent concealment by the defendants in order to avoid the four year statute of limitations for federal antitrust claims.

belated willingness to join in this particular action provides no assurance whatsoever of aggressive antitrust enforcement in other cases. *Id.* at A10.

Judge Posner contends that indirect purchaser consumers benefit from concentrating recovery in the hands of direct purchaser middlemen. *See* R. Posner, *Economic Analysis of Law* 294-95 (3rd ed. 1986). He also questions whether state attorneys general are truly vigorous advocates on whom society can rely to enforce the antitrust laws:

> Given the political character of *parens patriae* enforcement, it is doubtful that it can be relied upon as an adequate antitrust deterrent. There may well be a tendency under *parens patriae* for state attorneys general to bring headline-grabbing, scapegoat-seeking suits against politically unpopular corporations, with little regard for the intrinsic antitrust merit of the suit and with little effort to press the suit to a successful conclusion. By the time the case is ready for trial, the state attorney general's office may be occupied by a new politician with little interest in carrying out the projects of his predecessor.

W. Landes & R. Posner, *Should Indirect Purchasers Have Standing to Sue Under the Antitrust Laws? An Economic Analysis of the Rule of Illinois Brick*, 46 U. Chi. L. Rev. 602, 613 (1979).[12]

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[12] *See also* Minority Report on P.L. 94-435, H.R. Rep. No. 94-499, 94th Cong., 2d Sess. 24-25, *reprinted in* 1976 U.S. Code Cong. & Ad. News 3, 2593. ("We believe that politics and antitrust will not make a happy marriage. The temptations for the politically ambitious to ride into the public eye as its champion against "fat cat" antitrust violators by filing lawsuits to the sound of political trumpets may be too great. Since antitrust cases take years to complete, the politically ambitious

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In addition, because "[t]he antitrust units of the states are generally understaffed and subject to budgetary constraints," state attorneys general are often unable to follow through with the trial of antitrust cases. T. Wilson, *Defending An Antitrust Action Brought By a State AG*, 1 A.B.A. Antitrust 10, 14 (1987).[13]

Neither Missouri nor Kansas pursued this case until KPL completed the thorough investigation necessary to evaluate and file a complex antitrust suit. KPL actually encouraged the Attorneys General of Missouri and Kansas to enter the case on behalf of municipal utilities served by the Pipeline. This litigation proves that federal antitrust enforcement responsibility should not be splintered among direct purchasers and state attorneys general bringing *parens patriae* claims on behalf of indirect purchaser consumers.

The possibility that state public utility commissions may threaten to take away all incentives from the utilities by passing through all damages they recover to the

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attorney general need not fear the embarrassment of a string of losses. In any event, many of the cases will have been undoubtedly settled because of their adverse publicity and their nuisance value.").

[13] Footnote 9 on page 19 of the Amici Brief of the Forty-Six States underscores this point. Of the seven cases cited as support for the "powerful and effective weapon" of *parens patriae* suits, all were settled.

The states claim great expertise in enforcing the antitrust laws, Forty-Six States' Amici Brief at 21, but neglect to mention that in this case both Kansas and Missouri have hired private attorneys to prosecute their claims.

consumers is largely within the states' control. If the States fear that these utilities lack a sufficient incentive to pursue claims against antitrust violators, then the answer lies in rewarding utilities for their initiative by allowing their stockholders to keep the treble damages portion of the recovery. Alternatively, the regulatory commissions could punish utilities who refuse to pursue meritorious antitrust suits by refusing to allow them to pass on overcharges or by forcing them to turn some portion of the overcharges to the customers.

Petitioners cannot be permitted to strip the utilities of their motivation to sue and then to contend that the disincentive created by the States justifies *parens patriae* claims on behalf of indirect residential purchasers. Moreover, federal antitrust policy should not be held hostage to the relationship between a state utility commission and either the utilities it regulates or the state's attorney general.

The goals of the antitrust laws in recouping illegal overcharges and punishing wrongdoers will best be served by allowing UtiliCorp, KPL, and the municipal utilities to pursue their direct purchaser antitrust claims against the defendants.

III. NO EXCEPTION TO THE DIRECT PURCHASER RULE SHOULD BE RECOGNIZED IN THIS CASE.

In an effort to keep their *parens patriae* claims alive, petitioners seek to wring from *Illinois Brick* an exception based on the regulated nature of the natural gas industry. The short answer to their argument is that no exception is

needed in this case to serve the policies of the antitrust laws.

Although a "cost-plus" exception to the "no pass-on" rule might apply when the direct purchaser "has not been damaged," *Hanover Shoe*, 392 U.S. at 494, UtiliCorp has alleged damages which this Court has concentrated solely in the hands of direct purchasers. This Court specifically recognized in *Hanover Shoe* that direct purchasers would incur recoverable damages if total sales declined as a result of illegal overcharges. *Id.* at 493.

In *Illinois Brick*, the Court explained that the cost-plus exception to the rule barring offensive and defensive use of pass-on theories applies only if "the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." *Illinois Brick*, 431 U.S. at 736. The hypothetical cost-plus exception mentioned in *Illinois Brick* does not apply in this case because UtiliCorp's customers do not purchase natural gas under preexisting, fixed quantity contracts. *See Wyoming Tight Sands*, A34, *aff'd*, A12.

Other courts have also recognized the requirement of a fixed quantity contract between direct and indirect purchasers before the pass-on defense can be asserted. *See Jewish Hospital Ass'n v. Stewart Mechanical Enterprises, Inc.*, 628 F.2d 971, 976 (6th Cir. 1980), *cert. denied*, 450 U.S. 966 (1981); *Mid-West Paper Products Co. v. Continental Group, Inc.*, 596 F.2d 573, 577 n.9 (3rd Cir. 1979); *Eastern Air Lines, Inc. v. Atlantic Richfield Co.*, 609 F.2d 497, 498, 499 (Emer. Ct. App. 1979); *Lefrack v. Arabian American Oil Co.*, 487 F. Supp. 808, 818-20, 822-23 (E.D.N.Y. 1980).

The rationale behind the cost-plus exception to *Illinois Brick* focuses on whether a direct purchaser can require its customers to buy a fixed quantity, thereby permitting the direct purchaser to pass through an illegal price increase without suffering ill effects. Where the indirect customers are obligated to buy a fixed quantity of product regardless of price increases, the distributor is completely shielded from damage resulting from the illegal overcharge. Only with cost-plus contracts for fixed quantities can courts be sure that the direct purchaser is not damaged.

That rationale does not apply in this case. UtiliCorp's customers purchase only that amount of natural gas which satisfies their individual needs and budgets. As testimony in the case confirms, consumers decrease their purchases in response to higher prices.

The Court should reject the reasoning of the Seventh Circuit in *Panhandle Eastern* applying a cost-plus exception to the direct purchaser rule in the absence of a fixed quantity purchase. Regulated public utility markets do not justify different ground rules for recognition of a cost-plus exception. *See Illinois Brick*, 431 U.S. at 743-44. Because increased natural gas costs have affected both UtiliCorp's volume of resold gas and its profits in accordance with the market forces of supply and demand, the creation of a regulatory equivalent to the cost-plus exception based on public utility regulation would be a mistake that would weaken enforcement of the antitrust laws.[14]

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[14] If the Court were inclined to create a public utility pass-on exception to the direct purchaser rule, UtiliCorp's recovery

(Continued on following page)

IV. THE STATES' BELATED RELIANCE ON SECTION 4c OF THE CLAYTON ACT DOES NOT BAR UTILICORP'S SECTION 4 CLAIMS.

A. The States' Section 4c Argument Violates Supreme Court Rule 24.1(a).

In their brief on the merits, petitioners urge the Court to reverse the Tenth Circuit's judgment for the "separate reason" that Section 4c of the Clayton Act authorizes *parens patriae* actions on behalf of indirect purchasers. Until this Brief, the States have never argued that Section 4c provides an alternative substantive reason for avoiding the bar of *Illinois Brick*.

The States' failure to raise Section 4c in their briefs filed in the District Court, in their Tenth Circuit brief and oral argument, and in their petition for a writ of

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of overcharge damages attributable to its commercial and industrial customers should remain unaffected by the Seventh Circuit's opinion in *Panhandle Eastern*. Judge Posner recognized that the industrial market for natural gas differs substantially from the residential customer market. *Panhandle Eastern*, A58.

Because industrial customers possess fuel-switching capabilities, Judge Posner argued that public utilities do not exercise the degree of monopoly power over customers which served as the rationale for the Seventh Circuit's "regulatory" equivalent to a possible cost-plus exception. Given a different factual record, the Court was not required to sacrifice the overcharges passed on to the utility's commercial and industrial customers – in stark contrast to the elimination of more than 50% of the damages claimed by the utilities in this case which would occur if the States' pass-on theories were permitted.

certiorari[15] forecloses consideration of that question as part of petitioners' brief on the merits. *See* Supreme Court Rule 24.1(a). *See also United States v. Lovasco,* 431 U.S. 783, 788 n.7 (1977); *Neely v. Martin K. Eby Construction Co.,* 386 U.S. 317, 330 (1967); *Duignan v. United States,* 274 U.S. 195, 200 (1927).

In their petition, the States sought a writ of certiorari to resolve one "critical question":

> Do indirect purchasers, who by regulatory mandate pay *all* of the illegal antitrust overcharges, fall within an exception to the general rule that only direct purchasers of a product have standing to seek antitrust damages from antitrust violators. The Seventh Circuit says "yes"; the Tenth Circuit says "no".

Petition at 8 (emphasis in original).

Those "yes" or "no" answers were to the question of whether a regulatory cost-plus exception to the Clayton Act may exist under *Hanover Shoe* and *Illinois Brick.* Neither the Seventh Circuit in *Panhandle Eastern* nor the Tenth Circuit in this case was presented with a Section 4c argument, and neither of the petitions for writs of certiorari addressed that issue.

Throughout the briefing and argument in the Courts below, the States have focused exclusively on the proposed cost-plus exception to *Illinois Brick* to the exclusion of any consideration of Section 4c of the Clayton Act. Petitioners' effort to divert the Court's attention to an issue not raised in the District Court or in the Tenth Circuit is improper under Supreme Court Rule 24.1(a).

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[15] In their petition, the States did not even cite Section 4c of the Clayton Act as a "statute involved in the case."

B. Section 4c Of The Clayton Act Does Not Bar UtiliCorp's Section 4 Claims.

Even if the Court were to consider petitioners' Section 4c argument on the merits, *parens patriae* causes of action do not bar UtiliCorp's claims under Section 4 of the Clayton Act. The *parens patriae* mechanism creates nothing more than "a new procedural device" to enforce existing rights of recovery under Section 4. *Illinois Brick,* 431 U.S. at 733-34 n.14. *See also In re Coordinated Pretrial Proceedings in Petroleum Products Antitrust Litigation,* 691 F.2d 1335, 1340 (9th Cir. 1982), *cert. denied sub nom. California v. Standard Oil Co.,* 464 U.S. 1068 (1984); *State of New York v. Dairylea Co-op, Inc.,* 570 F. Supp. 1213, 1215 (S.D.N.Y. 1983).

Congress' overriding purpose in enacting Section 4c was to provide state attorneys general with the power to enforce consumers' *existing* rights of recovery under Section 4.[16] In accordance with this intent, Congress included a notice provision in Section 4c for persons on whose behalf a *parens patriae* action is brought so that they could opt out of the case.[17] There would have been no reason

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[16] Taking half a sentence from a 1982 opinion out of context, petitioners erroneously assert that this Court has concluded that indirect purchaser suits are allowed under the Hart-Scott-Rodino Act because an indirect purchaser remedy "already existed." Petitioners' Brief at 29 n.19, *quoting Merrill Lynch, Pierce, Fenner & Smith v. Curran,* 456 U.S. 353, 378 (1982). Instead of addressing *parens patriae* claims under Section 4c, *Merrill Lynch* arose out of private party claims under the Commodity Exchange Act.

[17] In this case, the States of Missouri and Kansas have never followed the requirements of 15 U.S.C. § 15c(b)(2) by providing a notice to consumers of their right to opt out.

for Congress to provide an "opt out" method for claims for which consumers had no cause of action. Moreover, if Congress had intended to give state attorneys general independent standing under federal antitrust laws, it would not have limited *parens patriae* claims to recovery only on behalf of those individuals who declined to opt out of the antitrust suit.

The States rely on the language and the legislative history of the Hart-Scott-Rodino Act to support their misinterpretation of Section 4c. Neither the Act itself nor the debates which preceded its passage support petitioners' statement that "[t]he Act cannot sensibly be read as authorizing *parens patriae* actions only on behalf of direct purchasers." Petitioners' Brief at 24.

When the Act was passed in 1976, this Court had not addressed the question of whether *Hanover Shoe's* rejection of the pass-on defense would be applied symmetrically to bar the claims of indirect purchasers. This Court resolved that ambiguity in 1977 in *Illinois Brick,* explicitly considering and rejecting the notion that Congress had intended for indirect purchasers to sue under Section 4c, but not under Section 4:

> Congress made clear . . . that this legislation did not alter the definition of which overcharged persons were injured within the meaning of § 4. * * * Representative Rodino himself acknowledged . . . that this legislation did not create a right of recovery for consumers where one did not already exist. * * * [W]e think the construction of § 4 adopted in [*Hanover Shoe*] cannot be applied for the exclusive benefit of plaintiffs. Should Congress disagree with this result, it may, of course, amend the section to change it. But it has not done so in the recent *parens patriae* legislation.

Illinois Brick, 431 U.S. at 733-34 n.14 (1977).[18]

In the thirteen years since *Illinois Brick,* Congress has repeatedly refused to amend Section 4c to overrule that opinion. Several state attorneys general have testified that legislative change is necessary because Section 4c does not create new remedies under the Clayton Act for *parens patriae* claims and *Illinois Brick* bars their *parens patriae* claims on behalf of indirect purchasers. *See Fair and Effective Enforcement of the Antitrust Laws, S. 1874: Hearings on S. 1874 before the Subcommittee on Antitrust and Monopoly of the Senate Judiciary Committee,* 95th Cong., 1st Sess. 124 (1977) (Prepared statement of the California Attorney General) ("*Illinois Brick* . . . has virtually destroyed the right of indirect purchasers to recover damages under federal antitrust laws and has thereby seriously crippled the power of the States to enforce the antitrust laws pursuant to the recently enacted *parens patriae* legislation."); *id.,* 95th Cong., 2d Sess. at 109 (1978) (statement of the Arizona Attorney General). *See also Effective Enforcement of the Antitrust Laws, H.R. 8359: Hearings on H.R. 8359 Before the Subcommittee on Antitrust and Monopoly of the House Judiciary Committee,* 95th Cong., 1st

[18] In footnote 14 to *Illinois Brick,* the Court cited to a brief filed by 47 States as amici curiae. In that brief, the states argued that *all* indirect purchasers should be permitted to maintain antitrust claims. They lost. In handing the states that defeat, this Court anticipated – and rejected – their argument in this case that liability standards of Section 4 differ from those of Section 4c.

Sess. 476 (1977) (letter from Washington's Attorney General Slade Gordon).

In lobbying Congress to amend Section 4c to allow for suits on behalf of indirect purchasers, state attorneys general have relied principally on an argument that, in the wake of *Illinois Brick*, the federal *parens patriae* statute does not permit them to use Section 4c to represent consumers who could not assert individual claims. They believed that *Illinois Brick* precludes them from representing indirect purchaser consumers.

In an unsuccessful attempt to respond to the states' concerns, the Senate Judiciary Committee recommended a remedial bill with these comments:

> [T]he majority opinion in *Illinois Brick* has emasculated *parens patriae*. [It] permits no other conclusion. If most consumers are indirect purchasers, and indirect purchasers are barred from suit, and the *parens patriae* provisions merely create "a new procedural device * * * to enforce existing rights," it follows by tautology that the *parens patriae* rights of State attorneys general are no greater than the underlying rights of consumers. * * * *The State attorneys general have uniformly reached that conclusion.*

S. Rep. No. 239, 96th Cong., 1st Sess. 25-26 (1979) (emphasis added). *See also* 129 Cong. Rec. H1549 (daily ed. March 22, 1983) (remarks of Representative Peter W. Rodino) (hereinafter cited as "129 Cong. Rec. H1549").[19] Congress'

[19] The States contend that in Section 4c, "Congress intended to authorize state attorneys general to sue as *parens patriae* on behalf of indirect purchaser consumers," Petitioner's Brief

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refusal to amend the Clayton Act to reverse *Illinois Brick's* impact on Section 4c claims suggests that Congress is satisfied with *Illinois Brick* and does not desire to amend Section 4c to authorize *parens patriae* actions on behalf of indirect purchasers.

Finally, the States' reliance on the language of Section 4c is misplaced. The Act provides, in relevant part:

> . . . the court shall exclude from the amount of monetary relief awarded in such [*parens patriae*] action any amount of monetary relief (A) which duplicates amounts which have been awarded for the same injury, or (B) which is properly allocable to . . . (ii) any business entity.

Section 4c(a)(1) of the Clayton Act, 15 U.S.C. § 15c(a)(1) (1982). As a direct purchasing business entity, UtiliCorp stands first in line to recover overcharge damages under Section 4 of the Clayton Act.

Under both Sections 4 and 4c of the Clayton Act, UtiliCorp is the proper party to recover overcharge damages resulting from the defendants' anticompetitive conduct. Consumers are ultimately protected by the rule of *Illinois Brick* because the goals of avoiding complexity and duplication of damages and of vigorous enforcement

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at 26, citing Representative Rodino's remarks in the 1976 debates. Even if this Court had not already rejected that contention in footnote 14 of *Illinois Brick*, Representative Rodino's later statements in the 1983 debates on his proposed amendments to Section 4c demonstrate his agreement that "*Illinois Brick* negated this authority of State attorneys general" to sue on behalf of indirect purchasers. 129 Cong. Rec. H1549.

of the antitrust laws are best served when antitrust claims are asserted by direct purchasers.

CONCLUSION

The decision of the Court of Appeals should be affirmed.

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No. 88-2109

In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI, AS *PARENS PATRIAE*,

Petitioners,

v.

UTILICORP UNITED, INC.,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

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REPLY BRIEF FOR THE PETITIONERS

I. *ILLINOIS BRICK* SHOULD NOT BAR THE STATES' CLAIMS ON BEHALF OF RESIDENTIAL CONSUMERS WHO INCURRED THE ENTIRE ILLEGAL OVERCHARGE.

Petitioners are not seeking to overturn the *Illinois Brick* direct purchaser rule, or even to limit it in any significant way. The States instead merely suggest what the Court has already tacitly acknowledged – that in the

limited situation where indirect purchasers have demonstrably incurred the entire overcharge on the natural gas they bought, the *Illinois Brick* rule should not bar their claims.[1]

The Court has already recognized that there may be factual settings where the *Illinois Brick* rule should not mechanically preclude suits by indirect purchasers. These hypothetical settings – such as a "pre-existing cost-plus contract"[2] or a "cost-plus" contract for a fixed quantity[3] – seem to have been chosen only to ensure the *result* that the entire overcharge be passed on in identifiable form, so that complex issues of apportionment can be avoided.[4] Here that result already exists – the residential consumers *did* bear the entire overcharge.[5] The consumers should be allowed to recover the damages that they alone sustained.

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[1] Indeed, in these limited circumstances it is *Illinois Brick* that is the exception to the fundamental rule of Section 4 of the Clayton Act that *any* person sustaining antitrust injury may sue to recover therefor.

[2] *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481, 494 (1968).

[3] *See Illinois Brick Co. v. Illinois*, 431 U.S. 720, 735-36 (1977).

[4] *See California v. ARC America Corp.*, ___ U.S. ___, 109 S. Ct. 1661, 1666 n.6 (1989) ("[I]ndirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them."); *see also Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Co.*, 852 F.2d 891, 897 (7th Cir.) (en banc), *cert. denied*, 109 S.Ct. 543 (1988).

[5] Respondent and the amicus Washington Legal Foundation argue at length that all the overcharge may not have been passed on, or may somehow have been passed on imperfectly. Such fact-specific arguments are not proper because both lower

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It is ironic in light of the Court's expressed preference in *Illinois Brick* and *Hanover Shoe* for "the real economic world rather than an economist's hypothetical model," 431 U.S. at 732, that respondent and the supporting amici are urging the application of abstract economic theories to deny standing to the residential consumers. There is no need for abstract theory here because in the "real economic world" of this case there actually is a complete and easily provable pass through to residential consumers of the full overcharge paid by the utilities.[6]

Respondent erroneously argues that this case will become unreasonably complex unless the direct purchaser rule is applied. However, the outcome of this

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courts *assumed* a perfect and easily provable pass through of overcharges. Pet. App. A14; A33-34. Indeed, it was respondent UtiliCorp's motion for summary judgment that required such an assumption. This case thus presents the purely legal issue of whether an indirect purchaser who incurs a complete, readily-provable overcharge may sue under *Illinois Brick*.

[6] The United States suggests that a "closer question" would be presented where the direct purchaser "is subject to a written, legally binding obligation to pass on the entire amount of the overcharge," Br. at 26, and further acknowledges that "such an obligation could arise in many ways, including statute, regulation, contract and filed tariff." *Id.* at 26 n.30. But such a legally binding obligation is precisely what this case presents. Here all the overcharges were passed on to residential customers in accordance with the PGA pricing mechanism. As the *Panhandle Eastern* court noted, "for every cubic foot of gas bought by a residential customer, we *know* that the whole overcharge was passed on to the customers in accordance with the fuel pass-through provision of their contract . . . , and we know why (regulation plus the residential consumers' lack of alternatives)." 852 F.2d at 898.

appeal will have no appreciable effect on the complexity of the underlying suit.[7] All antitrust suits are complicated, and this one is no exception – it already contains numerous parties, and numerous claims not only for overcharges, but also for the utilities' lost profits. It will not make the case more complex simply to recognize that each of these discrete claims should belong to the real party in interest – the lost profits to the utilities, and the overcharges to the consumers who actually bore them. Rather, it will promote antitrust enforcement by ensuring that the injured parties rather than the "middlemen" utilities will be compensated.[8]

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[7] Respondent UtiliCorp sets forth an exhaustive litany of claims and parties at pp. 15-19 of its Brief, implying that this Court's ruling can somehow simplify this case for the jury. Br. at 17. The truth is that *all* these claims, and *all* these parties (including the States), will remain in the case regardless of how this Court rules.

[8] Respondent and the United States both implicitly concede that the antitrust goal of compensating injured parties will not be furthered in this case if the utilities are allowed to prosecute the indirect purchasers' claims. Nor can the utilities make a convincing case that they have greater incentive to sue than the States. Here UtiliCorp did not prosecute this case vigorously – it instead *dismissed* its suit in 1986 and did not seek to intervene again for over one year. *See* J.A. at 1. This voluntary dismissal subjects UtiliCorp (and thus any indirect purchasers it seeks to represent) to a serious threat from a statute of limitations defense that the States, which filed in 1985 and 1986, do not face. The doubtful prospect that a public utility commission will allow utilities to keep double or triple damages also cannot provide utilities with any real incentive to sue; the United States' unsupported suggestion to the contrary, Br. at 25, reflects a woeful misunderstanding of how public utility regulation operates.

Respondent and the United States also suggest that the claims of various industrial and commercial customers may be lost if the direct purchaser rule is not applied. The States have never advanced this argument, nor does the record support it.[9]

The extreme position on the direct purchaser rule is being advance here not by the States, but by respondent, and particularly by the United States. The Solicitor General suggests that if a direct purchaser can allege *any* antitrust injury, no matter how small, that direct purchaser should be allowed to recover all damages, *including overcharges that were completely passed on*. *See, e.g.*, United States Br. at 6.[10] This argument as a practical

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[9] UtiliCorp in fact argued to the contrary below. *See* Brief of Appellee UtiliCorp United Inc., filed in the Tenth Circuit on September 19, 1988 (J.A. 7), at 20-21. Moreover, as Judge Posner reasoned in *Panhandle Eastern*, the fuel-switching capabilities of industrial and commercial consumers make it unlikely that the entire overcharge will be passed on to them. 852 F.2d at 898. In these circumstances, in order to avoid the complex battle over apportionment that the Court rejected in *Illinois Brick*, the utilities as direct purchasers *should* prosecute these claims.

[10] The United States is able to make this argument only by wrenching the words "has not been damaged" in *Hanover Shoe* out of all context. *See* United States Br. at 7. The United States' argument necessarily ignores language in *Illinois Brick* and *ARC America* indicating that the Court's concern was not with separate claims for overcharges and lost profits, which are well recognized in antitrust law. The Court was instead concerned about the difficulty of apportioning the *overcharge itself* among various levels of direct and indirect purchasers. *See Illinois Brick*, 431 U.S. at 737; *ARC America*, 109 S.Ct. at 1666 n. 6.

matter means that the *Illinois Brick* rule will be absolutely without exception. Even where a textbook "pre-existing cost-plus contract" for a *fixed quantity* exists, the direct purchaser may still be damaged, as the United States itself recognizes. *See* United States Br. at 9 n.4 ("A direct purchaser may be damaged despite the existence of a cost-plus, fixed quantity contract – for example, if there is imperfect compliance with the contract."[11] The United States' position would encourage direct purchasers to assert *de minimis* claims so that they could reap windfall recoveries of overcharges that were fully passed on.

Petitioners are not seeking to revoke the direct purchaser rule of *Hanover Shoe* and *Illinois Brick*.[12] But where

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[11] Further, as Judge Posner noted in *Panhandle Eastern*, "the seller under a fixed-quantity cost-plus contract might forebear to insist on a 100% pass through in order to curry favor with the buyer for the sake of future deals." 852 F.2d at 898. It is not difficult to imagine other *de minimis* claims for damages by direct purchasers, such as one based on the time lag between the date the overcharge was incurred and the date payment for a 100% pass on was received.

[12] The States do find it curious that United States is now attempting to argue that the direct purchaser rule is "long standing" and has been consistently applied since at least 1906. United States Br. at 12. Not only does this argument ignore a host of lower court opinions, as well as this Court's post-*Illinois Brick* focus on "tangible economic injury" in *Blue Shield of Virginia v. McCready*, 457 U.S. 465, 475 n. 11 (1982), it contradicts the government's own position in 1976 in *Illinois Brick*. There, on complicated facts that fully justified this Court's concerns about injecting unwieldy apportionment issues into antitrust litigation, the United States urged that indirect purchaser claims be *allowed*.

indirect purchasers have admittedly incurred all of a challenged overcharge, the rule cannot sensibly be applied.

II. THE STATES' *PARENS PATRIAE* CLAIMS ARE AUTHORIZED BY CONGRESS AND WERE NOT FORECLOSED BY *ILLINOIS BRICK*

The Hart-Scott-Rodino Antitrust Improvements Act (the "Act") expressly authorizes the States' *parens patriae* actions.[13] Although respondent correctly recognizes that the Act was intended "to enforce consumers' *existing* rights of recovery under Section 4," Br. at 29 (emphasis original), respondent overlooks the fact that the Act was passed in 1976 – prior to *Illinois Brick* – when suits by indirect purchasers were still allowed by the federal

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[13] Respondent and the United States' argument that this issue is not properly before the Court lacks merit. The States' complaints specifically reference the *parens patriae* authority of the attorneys general. *See* Petition for Writ of Certiorari at 4 n.3. The extent of that authority was addressed by the Tenth Circuit, which "assume[d] that [it] comes into play when the individual consumers are the direct purchasers." Pet. App. A7 n.1. The issue was fairly included within Question 1 of the States' petition, which begins: "Do residential indirect purchasers of natural gas, represented *parens patriae* by their state attorneys general, have standing to sue . . . . " Because this pure issue of law was raised in the States' complaints, acknowledged by the Tenth Circuit, and fully briefed by the parties and amici, it is ripe for resolution by the Court. *See Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 697-98 (1984); *Nixon v. Fitzgerald*, 457 U.S. 731, 743 n. 23 (1982). Even if this important issue had not been properly raised, however, the Court may still address it. *See United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 371 n. 4 (1967)

courts. *See, e.g., In re Western Liquid Asphalt Cases* (and cases cited therein), 487 F.2d 191, 197 (9th Cir. 1973), *cert. denied sub nom., Standard Oil Co. of California v. Alaska*, 415 U.S. 919 (1974). Congress clearly assumed that the "consumers' *existing* rights" *included* indirect purchaser suits.

The legislative history of the Act demonstrates not only Congress' understanding in 1976 that indirect purchaser suits were allowed, but also its intent that such claims be part of the *parens patriae* authority of state attorneys general.[14] Congress' intent in 1976 is controlling as to Section 4C, despite the subsequent interpretation of Section 4 announced in *Illinois Brick*. *See Cannon v. University of Chicago*, 441 U.S. 677, 694-704 (1979).

Respondent and the United States erroneously infer from footnote 14 of *Illinois Brick* that the Court has already addressed and rejected the arguments raised here. But the Act was cited there only as evidence of congressional intent to allow indirect purchaser suits under Section 4 of the Clayton Act, not Section 4C. *See* United States Br. at 23-24 n.27. The Court rejected that argument without addressing whether the Act *itself* authorizes

[14] The United States has recognized that Congress intended to authorize *parens patriae* suits on behalf of indirect purchasers. *See* United States Br. at 23-24, n. 27 (summarizing the argument it made in *Illinois Brick* that the Act "allows indirect purchasers to recover overcharges passed through by direct purchasers (as shown in the legislative history of [the Act] and the policy considerations underlying that provision)").

attorneys general to bring *parens patriae* suits on behalf of indirect purchasers. That issue is one of first impression.[15]

Respondent also relies on Congress' failure to amend the Act in the years since *Illinois Brick* as evidence of congressional approval of the decision. However, as the Court noted in *Illinois Brick*, the interpretation of a statute cannot be altered by the action or inaction of subsequent legislators. 431 U.S. at 733 n.14. Further, Congress' failure to overrule *Illinois Brick* may be due to political reasons wholly unrelated to the case. Respondent's arguments to the contrary are pure speculation. *See Johnson v. Transportation Agency*, 480 U.S. 616, 671-72 (1987) (Scalia, J., dissenting).

Congress intended the Act to allow state attorneys general to bring antitrust suits on behalf of indirect purchasers. The legislative history could not be clearer. The Court should decide this case of first impression in favor of the States and allow the *parens patriae* claims to proceed.

[15] The United States argues that the Court in *Illinois Brick* *implicitly* rejected the argument that the Act authorizes *parens patriae* suits on behalf of indirect purchasers. But as the Solicitor General's brief makes plain, the court in *Illinois Brick* was asked to reason by analogy that because (1) the 1976 Act authorizes indirect purchaser suits and (2) Section 4 of the Clayton Act, enacted in 1914, is similarly worded, then Section 4 also must authorize indirect purchaser suits. The Court rejected the conclusion that a 1976 Act could define a 1914 statute, without ever addressing whether the 1976 Act authorizes indirect purchaser suits.

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No. 88-2109

In the Supreme Court of the United States

OCTOBER TERM, 1989

KANSAS AND MISSOURI, ETC., PETITIONERS

v.

UTILICORP UNITED INC.

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*ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT*

**BRIEF FOR THE UNITED STATES
AS AMICUS CURIAE SUPPORTING RESPONDENT**

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QUESTION PRESENTED

Whether the Court should recognize an exception to the pass-on rule of *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968), and *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977)—that only an overcharged direct purchaser, and not a subsequent indirect purchaser, is entitled to recover antitrust damages—where the direct purchaser is required by regulation to pass on the full amount of any illegal overcharge to the indirect purchaser, or where the pass on is easily proven.

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INTEREST OF THE UNITED STATES

The United States and the Federal Trade Commission has primary responsibility for enforcing the federal antitrust laws. This case presents the question whether the Clayton Act, which has been construed to provide that only a direct purchaser may recover damages for an unlawful overcharge, nevertheless permits indirect purchasers to recover damages if the injured direct purchaser passes the overcharge on to them. The Court's resolution of that question may affect both federal antitrust enforcement and the extent to which private enforcement of the federal antitrust laws achieves its intended purposes; as a result, the United States and the Federal Trade Commission have a significant interest in its correct resolution. The Court previously recognized that interest when, at the petition stage, it requested the views of the United States.

STATEMENT

1. Respondent is a public utility. It and another utility (Kansas Power & Light Company) purchased natural gas from a pipeline company for their own use and for delivery to their customers. The utilities, along with other purchasers of natural gas from the pipeline, sued the pipeline and five natural gas producing entities under Section 4 of the Clayton Act, 15 U.S.C. 15. The utilities alleged that the pipeline and the producers had conspired to inflate prices in violation of the Sherman Act. They sought as damages both the amount of the overcharge and lost profits attributable to the decrease in the quantity of natural gas demanded by the utilities' customers as a result of the higher prices.

Petitioners Kansas and Missouri subsequently brought *parens patriae* actions against the same pipeline-producer defendants on behalf of residential consumers in those States who had purchased natural gas from the utilities.[1] These actions were consolidated with the utilities' suit.

2. Defendants answered that the utilities lacked standing to bring an antitrust suit. According to the pipeline-producers, the utilities had passed on any illegal price increase to their customers. This pass on was assertedly required by state regulations and tariffs filed with state utility commissions. Pet. 4.

The utilities moved for partial summary judgment with respect to this defense, and the district court granted their motions. It noted that in *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968), this Court held that a direct purchaser is damaged within the meaning of Section 4 of the Clayton Act, 15 U.S.C. 15, to the full extent of an overcharge even if the entire overcharge is passed on to customers. Pet. App. A25-A27. The district court further observed that although *Hanover Shoe* involved the defensive use of a pass-on theory, this Court later held in *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977), that offensive use of the pass-on theory by indirect purchasers seeking to prove damages is also barred. Pet. App. A27.

[1] The residential consumers on whose behalf petitioners sued include customers of other utilities but exclude the utilities' customers in other States. Petitioners did not sue on behalf of the utilities' customers who are not natural persons.

Petitioners also sued in a representative capacity on behalf of governmental entities that purchased natural gas from the pipeline. This aspect of the case is not at issue here.

The district court acknowledged that the extent to which the utilities in this case passed on the allegedly illegal overcharge was a disputed factual issue; however, the court concluded that the pass-on defense would be barred even "if the facts establish that the rate systems governing the utilities permitted a total pass-through of any price increase." Pet. App. A33. Although this Court had suggested that the pass-on rule might not apply when an overcharged buyer has a pre-existing "cost-plus" contract for a fixed quantity, *Illinois Brick*, 431 U.S. at 736; see *Hanover Shoe*, 392 U.S. at 494, the district court held this possible exception inapplicable because "consumer demand for natural gas is governed neither by a fixed-quantity contract nor by anything resembling its 'functional equivalent.'" Pet. App. A34. Recognizing that the utilities' motions "were, in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity," the district court dismissed petitioners' *parens patriae* claims. Pet. App. A38.

In its ruling, the district court relied on *Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Co.*, 839 F.2d 1206 (1988), where a panel of the Seventh Circuit had on "almost identical facts" rejected a similar pass-on contention. Pet. App. A36. After the district court rendered its decision, the Seventh Circuit granted rehearing en banc in *Panhandle Eastern*. In response, the district court certified to the Tenth Circuit the following question for interlocutory appeal:

> In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens*

> *patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?

Pet. App. A41.

3. The court of appeals answered the certified question in the negative. In its view, the reasoning of *Hanover Shoe* and *Illinois Brick* requires that the cost-plus exception—if there is one[2]—be limited to cases involving a pre-existing contract for a fixed quantity. Pet. App. A8. In the absence of a fixed quantity provision, the court reasoned, the utilities would presumably suffer injury from the decreased demand for natural gas resulting from the higher price even if they passed on the entire overcharge. Pet. App. A12-A13. Consequently, it would still be necessary to apportion damages between the direct and indirect purchasers, were the latter permitted to recover. Pet. App. A14. The court of appeals therefore concluded that even if there were "a perfect and provable pass-on of the allegedly illegal overcharge" in this case, *ibid.*, the cost-plus exception would not apply.

In the meantime, the en banc Seventh Circuit had reached a contrary conclusion in *Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (*reprinted at* Pet. App. A43-A65), cert. denied, 109 S.Ct. 543 (1988). The Tenth Circuit, however, expressly declined "to apply the law as enunciated in *Panhandle Eastern.*" Pet. App. A13.

SUMMARY OF ARGUMENT

In *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968), and *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977), this Court held that an injured

[2] The court noted that this Court had not said that a pre-existing cost-plus contract for a fixed quantity "would constitute an exception but rather that it 'might be.'" Pet. App. A8.

direct purchaser—and not a subsequent indirect purchaser—is entitled to recover the full measure of antitrust damages. That rule applies even if the injured direct purchaser passed on the full amount of the illegal overcharge to the indirect purchaser.

A. The Court did recognize that an exception might exist where the direct purchaser suffered no antitrust injury whatsoever, and that fact was easily proven. Such an exception might apply when the direct purchaser has a pre-existing cost-plus contract with a customer (the indirect purchaser) for a fixed quantity. But any such exception has no application here. The residential utility customers (on whose behalf the States sued as *parens patriae*) were under no obligation to maintain purchases of a fixed quantity of natural gas at the allegedly inflated price. Hence, respondent presumably lost profits from reduction in demand for natural gas as a result of the higher price.

Decisions of this Court and lower federal courts since 1906 have held that an injured direct purchaser is entitled to recover an overcharge (so that, conversely, an indirect purchaser is entitled to no recovery) as long as the direct purchaser suffered injury under Section 4. That rule applied regardless of whether the direct purchaser passed on the overcharge to its customer, the indirect purchaser. This rule greatly simplified antitrust litigation and facilitated enforcement of the antitrust laws. *Hanover Shoe* simply extended the rule by barring complicated and usually futile attempts to prove that the direct purchaser was not injured, thus further simplifying litigation and facilitating enforcement.

B. No exception to the rule barring indirect purchaser suits should be created for cases in which 100% of an overcharge is passed through to an indirect purchaser. Considerations of *stare decisis*, administrability, and antitrust policy impose a heavy burden on those who urge creation of an exception to the rule of *Hanover Shoe* and *Illinois Brick*. That burden cannot be satisfied here. A "100% pass-through" exception would be difficult to

prove, the addition of new parties would complicate litigation, and such an exception would dilute incentives to sue by jeopardizing compensation for those directly injured by an illegal overcharge. Limiting a "100%" pass-through" exception to regulated industries, or to circumstances in which the pass on is presumed to occur as a matter of law, does not sufficiently increase the benefits or reduce the costs of the exception.

ARGUMENT

A DIRECT PURCHASER THAT SUFFERS INJURY (AND ONLY THE DIRECT PURCHASER) IS ENTITLED TO RECOVER THE FULL MEASURE OF ANTITRUST DAMAGES EVEN IF IT PASSED ON AN OVERCHARGE TO ITS CUSTOMERS

The *Hanover Shoe/Illinois Brick* rule holds that an indirect purchaser cannot recover antitrust damages for an illegal overcharge passed through to it by an injured direct purchaser. Instead, only the direct purchaser can recover. Any possible exception to that rule—for pre-existing cost-plus contracts for a fixed quantity—does not apply in this case, because that exception is limited to the situation where it is simple to show that the direct purchaser was not injured *at all* by the overcharge. Proof of even a 100% pass on here would not establish lack of injury to the direct purchaser because, as petitioners concede, Br. 14-15, the direct purchasers (the utilities) may nevertheless have lost profits (by virtue of lost sales) and thus been injured. In addition, no applicable new exception can be justified consistent with *Illinois Brick*.

A. The Possible "Cost-Plus" Exception Would Only Permit An Indirect Purchaser To Sue When It Is Easy To Prove That The Direct Purchaser Was Not Injured At All By The Overcharge

At least since the first decade of this century, the antitrust laws have provided that a direct purchaser who pays a price unlawfully elevated by an antitrust violator

and is injured in his business or property is entitled to recover as damages the difference between the price paid and the price which would have prevailed but for the violation. The "cost-plus exception" hinted at by this Court in *Hanover Shoe* and *Illinois Brick* is not an exception to this rule at all. Rather, the "exception" would, in certain circumstances, simply permit proof that a direct purchaser has not in fact been injured. Here, there is no claim that the direct purchaser was not injured.

1. Hanover Shoe *And* Illinois Brick *Do Not Permit Indirect Purchasers To Sue For Antitrust Injury Damages Where The Direct Purchaser Suffered Injury*

Hanover Shoe rejected the pass-on defense to a suit by a direct purchaser except (perhaps) where it is "easy to prove" that the direct purchaser "has not been damaged" in his business or property under the antitrust laws. 392 U.S. at 494. *Illinois Brick* held that if a pass-on theory may not be used defensively by a defendant against a direct purchaser, it may not be used offensively by an indirect purchaser to sue the defendant. 431 U.S. at 728. Because petitioners' offer to prove that respondent passed through 100% of any overcharge to indirect purchasers fails to establish that respondent has "not been damaged" as required by *Hanover Shoe* (in the defensive context), and because defensive and offensive uses of the pass-on theory are to be treated equally according to *Illinois Brick*, petitioners' attempt to use the pass-on theory offensively here is foreclosed by *Hanover Shoe* and *Illinois Brick*.

a. In *Hanover Shoe*, plaintiff Hanover—a shoe manufacturer—alleged that defendant United—a manufacturer of shoe machinery—unlawfully refused to sell its machinery and only leased it, so that the cost to Hanover was higher than it otherwise would have been. Hanover sought to recover the overcharge as damages. For its part, United contended that Hanover was not injured and was therefore not entitled to recover under Section 4

of the Clayton Act, because any excess cost of leasing as opposed to purchasing "was not absorbed by Hanover but was transferred to its customers." Pet. Br. at 62, *United Shoe Machinery Corp.* v. *Hanover Shoe, Inc.*, No. 463 (1967 Term) (consolidated with *Hanover Shoe*).

This Court squarely rejected United's contention. The *Hanover Shoe* Court held that "when a buyer shows that the price paid by him for materials purchased for use in his business is illegally high and also shows the amount of the overcharge, he has made out a prima facie case of injury and damage within the meaning of § 4." 392 U.S. at 489. Moreover, "the buyer is equally entitled to damages if he raises the price for his own product," because by charging an unlawfully high price, the seller "takes from the buyer more than the law allows" and "[a]t whatever price the buyer sells, * * * his profits would be greater were his costs lower." *Ibid.* The Court thus rejected the defense to a suit by a direct purchaser that the full overcharge was passed through to its customers, the indirect purchasers. *Id.* at 492-494.

What is more, the Court refused as a general matter to entertain offers of proof that the direct purchaser suffered "no loss" at all from the overcharge. United had proposed to prove that 100% of the overcharge was passed through to indirect purchasers *and* that Hanover had suffered no lost profits from a "decline in sales" because "the demand for [its] products [w]as so inelastic" that a price increase in the full amount of the overcharge would not cause "a consequent decline in sales." 392 U.S. at 492. But the Court concluded that "in the real economic world rather than an economist's hypothetical model," *id.* at 493, the task "would normally prove insurmountable" because numerous factors influence pricing policies, the effect on sales of a change in price is difficult to determine, and the behavior of unit costs given a change in sales volume cannot reliably be measured, *id.* at 492-493. Rather than permit defendants needlessly to complicate antitrust litigation by attempting to prove that the plaintiff had suffered no injury, the Court generally barred the pass-on defense.[3]

The Court did, however, suggest that in exceptional circumstances the pass-on defense "might" be permitted and the overcharged direct purchaser's prima facie claim of injury rebutted "when an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged." 392 U.S. at 494. Because the Court had earlier in its opinion recognized that an overcharged plaintiff would be injured despite a complete pass on of the overcharge if its sales declined as a result of charging higher prices, *id.* at 493, a fixed quantity qualification was implicit in its references to a "'cost-plus' contract," since only then would it to be "easy to prove" that the plaintiff had not been injured.[4] The Court made this limitation explicit in *Illinois Brick*,[5] noting that with a cost-plus contract, "the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." 431 U.S. at 736.[6]

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[3] The Court briefly discussed additional policy considerations supporting its holding, 392 U.S. at 494, which we address below.

[4] Recognition of this possible exception is not compelled by the reasoning of *Hanover Shoe*. The cases on which the Court relied, see Point A.2, *infra*, appear to hold that payment of the overcharge as such is injury. Moreover, a direct purchaser may be damaged despite the existence of a cost-plus, fixed quantity contract—for example, if there is imperfect compliance with the contract.

[5] In *Illinois Brick* the Court also suggested another possible exception: "where the direct purchaser is owned or controlled by its customer." 431 U.S. at 736 n.16. In such cases, the direct and indirect purchasers are in reality but a single entity, and no reason in law or antitrust policy suggests that one rather than the other should be allowed to recover damages for the injury. Cf. *Copperweld Corp.* v. *Independence Tube Corp.*, 467 U.S. 752, 771-774 (1984).

[6] *Hanover Shoe* addressed the pass-on defense. *Illinois Brick* held that "whatever rule is to be adopted regarding pass-on in antitrust damage actions, it must apply equally to plaintiffs and defendants,"

b. The Tenth Circuit correctly interpreted the possible " 'cost-plus' contract" exception as "requiring a pre-existing cost-plus contract for a fixed quantity," Pet. App. A8, which is not present in this case. And it correctly perceived that, in the absence of a contract for a fixed quantity, there remained "the issue of decreased residential demand caused by the higher price," Pet. App. A12-A13, even if, as alleged, the utilities passed on the entire overcharge to their customers. Thus, a perfect pass on alone would not establish, as defendants had asserted, that the "plaintiffs had not been injured in their business or property," Pet. App. A4—the plaintiff utilities may well have lost profits because of declining volume resulting from a higher price. The indirect purchaser rule, therefore, provides that the utilities, as direct purchasers, may sue for the entire amount of the overcharge, and concomitantly that the indirect purchasers may not sue.

The Seventh Circuit in *Panhandle Eastern* reached a contrary conclusion only by overlooking the predicate of the cost-plus exception suggested in *Hanover Shoe* and *Illinois Brick*: that the direct purchaser not be injured at all as a result of an overcharge. Indeed, the Seventh Circuit conceded that the direct purchaser in *Panhandle* would have lost sales to residential customers as a result of the higher prices; in consequence, the direct purchaser would have suffered injury and could sue for damages. Pet. App. A54-A55.[7] The Seventh Circuit apparently believed that a cost-plus exception was justified where there is no need to apportion the incidence of an overcharge between a direct purchaser and indirect purchasers—*i.e.*, to determine the proportion of the overcharge borne by each class of purchasers. Pet. App. A50-A51, A55, A58. It concluded that other arrangements that may ensure a perfect pass on of the overcharge serve the same function as a pre-existing cost-plus contract for a fixed quantity, and therefore fall within the scope of the exception.[8]

Whatever the relevance of ease of apportionment to the decision whether to create other exceptions to the indirect purchaser rule, it is not the reason this Court articulated as a possible justification for a cost-plus exception. Indeed, the Court's opinion in *Hanover Shoe* did not mention the problem of apportioning the amount of the overcharge paid. And in *Illinois Brick*, this Court considered the apportionment problem in the context of whether it should "cut back or abandon the *Hanover Shoe* rule." 431 U.S. at 736; see *id.* at 740-742.[9] The Court suggested the possible cost-plus exception because a particular kind of contract made it easy to prove that the direct purchaser had not been damaged at all. The *Hanover Shoe* Court never even contemplated permitting both direct and indirect purchasers to sue, with a resulting need to apportion damages or restrict an injured direct

431 U.S. at 728, and declined to overrule or limit the rule of *Hanover Shoe*.

[7] The contention of amici Forty-Six States that "[a] regulatory scheme that provides for automatic pass-through of fuel price increases operates identically to a fixed-quantity cost-plus contract," Forty-Six States Amici Br. 14, is incorrect: such a contract—unlike the regulatory scheme—prevents loss of sales that would otherwise follow the increase in price. Amici tacitly recognize this difference when they present an alternative argument in the event that "residential customers reduce consumption in response to higher rates." *Id.* at 15. Similarly, petitioners expressly recognize "[t]he fact that the utilities may have lost sales." Pet. Br. 14.

[8] According to the Seventh Circuit, other arrangements serving this function include, at a minimum, not just regulatory provisions such as those at issue here, but also requirements contracts with cost-plus provisions. Pet. App. A57, A59.

[9] The Court's two brief discussions of the cost-plus exception in *Illinois Brick*, 431 U.S. at 724 n.2, 736, occurred prior to its introduction of apportionment concerns, see *id.* at 737. Illinois had contended that "[t]he masonry and general contractors are nothing more than conduits between defendants and plaintiffs. The contractors absorb none of the illegal overcharges, but recover it (and more) from the State of Illinois and its public agencies." Resp. Br. at 21, *Illinois Brick Co.* v. *Illinois*, *supra*. If that were true, there would have been no need to apportion the overcharge in that case even if Illinois had been permitted to sue for the overcharge.

purchaser to recovering his lost profits from diminished sales volume.

Thus, the Seventh Circuit's conclusion that the indirect purchaser rule, as formulated by this Court, can be interpreted to bar recovery of the overcharge by an injured direct purchaser is simply wrong. Whether or not there is an exception to the indirect purchaser rule for pre-existing cost-plus contracts for a fixed quantity, the Tenth Circuit correctly held that such an exception, as this Court has articulated its scope,[10] was not applicable here.

2. *The Rule That A Direct Purchaser May Recover The Entire Overcharge If The Overcharge Injured It (And Conversely, That An Indirect Purchaser May Not Recover In That Situation) Is Of Long Standing And Represents Sound Antitrust Policy*

Hanover Shoe and *Illinois Brick* were not *sui generis*. To the contrary, they represented the culmination of a line of decisions by the Supreme Court and lower federal courts which had repeatedly held that injured direct purchasers were entitled to recover the entire overcharge. *Hanover Shoe*, 392 U.S. at 489-492 & n.7. The decisions antedating *Hanover Shoe* and *Illinois Brick* confirm that the rationale underlying the cost-plus/fixed-quantity contract exception is that such a contract made it "easy to prove" that the direct purchaser "has not been damaged" at all by the unlawful overcharge. *Hanover Shoe*, 392 U.S. at 494. Accordingly, the pass-on defense succeeded in those earlier cases only when the direct purchaser suffered no injury or failed to prove injury.

[10] The Court's brief mention of the cost-plus exception in *California* v. *Arc America Corp.*, 109 S.Ct. 1661, 1663 n.2, 1666 n.6 (1989), does not indicate any change in the underlying rationale or scope of that exception. The Court specifically referred to footnote 12 of *Illinois Brick*, which in turn quotes the portion of *Hanover Shoe* making clear that the cost-plus exception has to do with proof that the direct purchaser " 'has not been damaged,' " 431 U.S. at 732 n.12 (quoting 392 U.S. at 494).

The rejection of the pass-on theory in cases presaging *Hanover Shoe* and *Illinois Brick* accords with considerations of sound antitrust policy. Those decisions allowed injured direct purchasers (and, assuming mutuality of offensive and defensive use of the pass-on theory, *only* direct purchasers) to elect to recover illegal overcharges rather than having to prove lost profits, which would have been necessary if the pass-on defense were allowed.[11] Given the opportunity to recover the overcharge, direct purchasers could be expected to (and did in fact) seek that measure of damages, because the overcharge invariably equalled or exceeded any lost profits,[12] and because such damages were relatively simple to prove.[13] By allowing direct purchasers to recover the entire overcharge, the decisions anticipating *Hanover Shoe* and *Illinois Brick* provided direct purchasers with ample incentive to sue, thereby encouraging enforcement of the antitrust laws and enhancing their deterrent effect.

a. This Court first stated the fundamental principle that injured direct purchasers are entitled to recover the overcharge in 1906, in *Chattanooga Foundry & Pipe*

[11] This Court recognizes the distinction between overcharge and lost profits measures of damages, and suggested in *Hanover Shoe* that where the plaintiff could not prove an overcharge, "establishing damages might require a showing of loss of profits to the buyer." 392 U.S. at 494.

[12] If the direct purchaser absorbs the entire overcharge, its lost profits equal the amount of the overcharge. If instead the direct purchaser chooses to pass on some or all of the overcharge, it presumably does so because that action leads to a smaller decrease in profits. Thus, the amount of the overcharge should always equal or exceed lost profits.

[13] The aggregate overcharge is equal to the overcharge per unit multiplied by the number of units bought. The only difficult quantity in the calculation is the per unit overcharge, but that computation must be made to quantify lost profits as well: a prerequisite to determining reduction in quantity demanded from higher prices is an estimate of how much higher that price was. See note 14, *infra* (difficulty of proving lost profits measure of damages).

Works v. *City of Atlanta*, 203 U.S. 390 (1906). The City of Atlanta, which operated "a system of waterworks, and furnished water to consumers, charging for same precisely as would a private corporation engaged in like business," *City of Atlanta* v. *Chattanooga Foundry & Pipeworks*, 127 F. 23, 25 (6th Cir. 1903), aff'd, 203 U.S. 390 (1906), bought pipe for the waterworks at prices inflated by a price-fixing conspiracy and then sued "to recover back, as damages, the sum of money unlawfully demanded and paid," *City of Atlanta* v. *Chattanooga Foundry & Pipe Co.*, 101 F. 900, 907 (E.D. Tenn. 1900)—in other words, the amount of the overcharge.

Although Atlanta presumably recouped some or all of the overcharge it paid by increasing what it charged consumers, the appropriate measure of damages appears not to have been questioned at trial or on appeal. Nevertheless, on appeal of a verdict awarding Atlanta "the difference between the price paid and the market or fair price that the city would have had to pay under natural conditions had the combination been out of the way," 203 U.S. at 396, both the court of appeals and this Court had occasion to discuss injury and damages. The court of appeals noted that if the effect of a price-fixing conspiracy were to restrain interstate commerce "by reason of its tendency to affect the volume of such trade, then the effect upon the business of one who has paid the enhanced price * * * must be to correspondingly affect the volume or profit of that business." Since the excessive price results from the unlawful combination, the buyer "is entitled to recover the damages thus sustained," for the statute provides "compensatory relief to such persons as shall sustain an injury in some * * * business whose volume or profit has been diminished." 127 F. at 27. Justice Holmes for this Court said that Atlanta "was injured in its property, at least, if not in its business of furnishing water, by being led to pay more than the worth of the pipe. A person whose property is diminished by payment of money wrongfully induced is injured in his property." 203 U.S. at 396.

In 1918, Justice Holmes further explained the reasons for permitting the victim of an overcharge to recover the amount of the overcharge without inquiry into whether it had been passed on to the victim's customers. *Southern Pac. Co.* v. *Darnell-Taenzer Lumber Co.*, 245 U.S. 531 (1918). In *Darnell-Taenzer*, the Interstate Commerce Commission had found that the defendant railroad had charged an excessive rate and ordered reparation of the excess. When the railroad did not pay, a company which had paid the overcharge to the railroad sued to recover it. The railroad, in perhaps the first reported use of the so-called "pass-on defense," claimed that the plaintiff was not entitled to recover because it had passed on the overcharge to its customers. Rejecting that defense, Justice Holmes explained:

> The general tendency of the law, in regard to damages at least, is not to go beyond the first step. As it does not attribute remote consequences to a defendant so it holds him liable if proximately the plaintiff has suffered a loss. The plaintiffs suffered losses to the amount of the verdict when they paid. Their claim accrued at once in the theory of the law and it does not inquire into later events.

Id. at 533-534. Moreover, Justice Holmes pointed to another reason not to inquire into the ultimate economic effect of the overcharge on the plaintiff, one which assumed greater significance in *Hanover Shoe* and *Illinois Brick*—"the endlessness and futility of the effort to follow every transaction to its ultimate result." *Id.* at 534.

b. Because the amount of lost profits attributable to an overcharge can be difficult to prove [14] and is invariably no more than the overcharge itself, victims of overcharges

[14] See, *e.g.*, *Central Coal & Coke Co.* v. *Hartman*, 111 F. 96 (8th Cir. 1901) (no recovery because lost profits held too speculative). See generally Harrison, *The Lost Profits Measure of Damages in Price Enhancement Cases*, 64 Minn. L. Rev. 751, 754-755 (1980) (difficulty of proving lost profits probably retarded development of private antitrust action).

have generally sued for the amount of the overcharge rather than for their lost profits, and courts have expressly approved that election. Thus, in *Straus* v. *Victor Talking Mach. Co.*, 297 F. 791 (2d Cir. 1924), plaintiffs did not "sue[] for damages due to loss of profits. Their position is that they were entitled to buy goods in a free market," *id.* at 802-803, but instead were compelled to buy phonograph records at a higher price for resale to their customers, and they sued for the overcharge. The court held that plaintiffs "were not forced to sue for damages for loss of profits, and thus run the risk of no recovery" because of difficulty of proof, *id.* at 803, and, citing, *inter alia*, *Chattanooga Foundry* and *Darnell-Taenzer*, affirmed the award of the overcharge as damages.[15]

Despite clear precedent supporting an injured direct purchaser's recovery of the full amount of an overcharge, defendants continued to offer the pass-on defense, with occasional success. But where the defense was successful, it was because the court concluded that the plaintiff had not been injured or had failed to prove injury. The lower courts, despite the fact of overcharge, addressed whether the direct purchaser suffered injury. For example, in the "oil jobber" cases, brought in the wake of the government's successful prosecution for price fixing in the oil industry, *United States* v. *Socony-Vacuum Oil Co., Inc.*, 310 U.S. 150 (1940), oil jobbers sought, without success, recovery for damages they allegedly suffered as a result of the price fixing conspiracy. After some jobbers' claims

[15] The court thus rejected defendant's argument that evidence tending to show that a claimed loss was only a temporary loss "which the plaintiff in the course of his business has actually recoupped [sic] or could reasonably have recouped, is obviously evidence that is directly relevant to the issue whether the plaintiff has actually and ultimately been 'injured in his business or property.'" Brief on Behalf of Defendant Victor Talking Mach. Co. at 140-141 as quoted in *Atlantic City Elec. Co.* v. *General Elec. Co.*, 226 F. Supp. 59, 62 n.11 (S.D.N.Y. 1964).

for damages on decreased margins failed when no such decline could be shown, see, *e.g.*, *Twin Ports Oil Co.* v. *Pure Oil Co.*, 119 F.2d 747, 750 (8th Cir.), cert Denied 314 U.S. 644 (1941),[16] other jobber plaintiffs sought instead to recover the amount of the overcharge on the gasoline they bought. These latter jobbers contended that they were entitled "to recover without proof that they suffered any pecuniary loss in their business or property," and "even though their margins or profits on the gasoline were not lessened by reason of the conspiracy." *Clark Oil Co.* v. *Phillips Petroleum Co.*, 56 F. Supp. 569, 570-571 (D. Minn. 1944), aff'd, 148 F.2d 580 (8th Cir.), cert. denied, 326 U.S. 734 (1945). The district court in *Clark Oil* noted that plaintiffs had "allege[d] and claim[ed] no injury to their business or property," 56 F. Supp. at 575, and granted summary judgment for defendants; the court of appeals affirmed.[17]

Pass-on defenses were rejected in a series of cases arising out of a price fixing conspiracy in the electrical equipment industry, largely on the authority of *Chattanooga* and *Darnell-Taenzer*. See, *e.g.*, *Commonwealth Edison Co.* v. *Allis-Chalmers Mfg.*, 335 F.2d 203 (7th

[16] The court in *Twin Ports* also distinguished such cases as *Darnell-Taenzer* on various grounds, but primarily to establish that plaintiff was required to show pecuniary injury. 119 F.2d at 750-751. Its holding rested on plaintiffs' "failure to show * * * damages * * * as a result of the illegal combination." *Id.* at 751. Similarly, in *Northwestern Oil Co.* v. *Socony-Vacuum Oil Co.*, 138 F.2d 967, 971 (7th Cir.), cert. denied 321 U.S. 792 (1943), the court distinguished the *Darnell-Taenzer* line of cases, held that a showing of pecuniary loss was required, and denied recovery on the ground that plaintiff had "wholly failed to prove any loss to its property or business."

[17] See also *Wolfe* v. *National Lead Co.*, 225 F.2d 427, 433-434 (9th Cir.), cert. denied, 350 U.S. 915 (1955); *Miller Motors* v. *Ford Motor Co.*, 252 F.2d 441, 448 (4th Cir. 1958). In *Wolfe*, the court concluded there was no evidence that prices were fixed at higher than competitive levels or that plaintiffs had been damaged by paying higher prices, so that there was no proof of injury. In *Miller*, the court found both that the charge had been passed on and that any decline in volume was conjectural.

Cir. 1964). Judge Feinberg's opinion in *Atlantic City Elec. Co. v. General Elec. Co.*, 226 F. Supp. 59 (S.D.N.Y. 1964), is particularly enlightening. In a suit brought by an electric utility to recover the overcharge on the purchase of electrical equipment at prices allegedly inflated by price fixing, the court refused to require discovery into plaintiffs' rate bases and rates of return on the ground that evidence that plaintiffs had passed on the increased costs on to their customers was irrelevant. Judge Feinberg began by noting that a party suing for antitrust damages had traditionally been permitted to recover loss of profits, increased costs of business transacted, or decrease in value of investment; that these categories of injury were not necessarily mutually exclusive; and that recovery could be had for all three, given appropriate evidence. *Id.* at 61. He then observed that "as a practical matter, recognition of the passing-on doctrine is tantamount to a repudiation of the 'increased costs' measure of damages and a limitation of the extent of recovery primarily to lost profits." [18] *Id.* at 61-62. Judge Feinberg found support for the distinction between lost profits and the amount of the overcharge, and for an antitrust plaintiff's right to recover the amount of the overcharge, in *Straus*, *Chattanooga*, *Darnell-Taenzer*, and other cases. *Id.* at 62-67.[19]

[18] If the overcharge paid is reduced by the amount of the overcharge passed on, the result is a measure of lost profits on business actually transacted, assuming other factors affecting profits are unchanged.

[19] Judge Feinberg also sought to distinguish the oil jobber cases on various grounds. For example, he noted that the oil jobbers were able to recover their increased costs quickly, while electric utilities could not and would be "deprived for a long period of time of capital which they could have used for other purposes." 226 F. Supp. at 69. This suggests that, assuming complete pass on of the overcharge and ignoring lost profits from declining volume, the oil jobbers in fact had not been injured, while the electric utility was injured.

Ultimately, however, Judge Feinberg concluded that if the oil jobber cases could not be distinguished, they were "inconsistent with what appears to be more compelling authority." 226 F. Supp. at 70. Finally, Judge Feinberg concluded that recognition of a pass-on defense was not required as a matter of public policy. *Id.* at 70-71.

The pass-on theory has barred recovery of the overcharge by a direct purchaser only when he has suffered no injury to his business or property, thus confirming that the possible cost-plus exception to this Court's general rejection of the pass-on theory in *Hanover Shoe* and *Illinois Brick* extends only to the case where it is "easy to prove" that the direct purchaser "has not been damaged." *Hanover Shoe*, 392 U.S. at 494.[20] History equally demonstrates the wisdom of allowing direct purchasers to sue for the overcharge rather than attempting to establish the far more difficult measure of damages from lost profits. By permitting direct purchasers to recover the overcharge, disallowance of pass-on theories has encouraged enforcement of the antitrust laws and enhanced their deterrent effect.

B. No Exception To The *Hanover Shoe/Illinois Brick* Rule Barring Recovery By Indirect Purchasers Should Be Created For The Circumstances Of This Case

The Court has not previously suggested the existence of an exception to the indirect purchaser rule that would apply in this case, where the direct purchaser's injury is undisputed. We nonetheless consider whether antitrust policy suggests that the rule of *Hanover Shoe* and *Illinois Brick* be cut back to accommodate recovery of an overcharge by indirect purchasers where regulation (or pre-

[20] The varying approaches of the lower courts to the pass-on theory prior to *Hanover Shoe* turned on their treatment of evidence of the direct purchaser's injury. *Hanover Shoe* resolved the question dividing the lower courts by presuming injury from the overcharge and permitting the presumption to be rebutted, if at all, only by a simple evidentiary showing that the direct purchaser had not been injured at all.

existing contract)[21] provides for complete pass on of the overcharge, even though neither contract nor regulation insulates the direct purchaser from injury.

Illinois Brick, in which the Court refused to cut back on the *Hanover Shoe* rule, provides the framework for evaluation of any proposed exception to that rule. First, *Illinois Brick* indicates that proponents of an exception must shoulder a heavy burden of justification, because "considerations of *stare decisis* weigh heavily in the area of statutory construction, where Congress is free to change this Court's interpretation of its legislation." 431 U.S. at 736. The burden of precedent would seem even heavier since *Illinois Brick*, for in that case the Court rejected "attempts to carve out exceptions to the *Hanover Shoe* rule for particular types of markets." 431 U.S. at 744. That is precisely what would have to be done here. Second, any exception should be limited to narrowly defined circumstances and specifically justified by policy considerations clearly distinguishing those circumstances, so that the exception does not "substantially erode the *Hanover Shoe* rule without justification." *Ibid.* Third, any potential exception should be evaluated in light of the antitrust policy objectives of deterring antitrust violations and compensating victims, and the deterrence objective should be considered in light of incentives to sue and limiting the complexity of litigation.[22]

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[21] Although petitioners address only regulatory pass through, they present no basis for distinguishing regulatory pass through from pass through pursuant to contracts the Seventh Circuit concluded had similar effects and should be treated similarly. See note 8, *supra*.

[22] The policy objective of avoiding multiple liability also figures prominently in *Illinois Brick*, 431 U.S. at 730-731. However, the Court in *Illinois Brick* saw this objective as relevant to whether offensive and defensive use of pass-on theories should be treated symmetrically. The Court held that they should be, and that holding is not at issue here. Consequently, multiple liability is merely a "residual possibility," 431 U.S. at 737 n.18, which, although it "justifies bringing potential and actual claimants together in one

1. *A "Regulatory/Contractual 100% Pass-Through" Exception Should Not Be Created*

In our view, an exception to the indirect purchaser rule which would apply when the injured direct purchaser *in fact* passed on 100% of the overcharge, pursuant to contract or regulatory requirement, cannot be justified. Any attempt to prove that there had in fact been a perfect pass through of the overcharge would "entail the very problems that the *Hanover Shoe* rule was meant to avoid." *Illinois Brick*, 431 U.S. at 745. Despite a contract or regulatory requirement providing for pass through, proving a perfect pass through can be difficult, as recognized by both the Tenth Circuit in this case[23] and the Seventh Circuit in *Panhandle Eastern*.[24]

Moreover, the complexity of litigation would be increased by an increase in the number of parties involved. Direct purchasers who passed on the entire overcharge would presumably still seek to recover their lost profits attributable to declining volume, as the utilities do

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action if possible," *ibid.*, has little bearing on the policy choices this case presents.

[23] "Any allocation of illegal overcharges to the residential consumers may require tracing the sale from the wellhead through each level of distribution in order to establish the amount of illegal gas costs actually paid by the consumers in each state, probably resulting in exactly that which the Supreme Court prohibited, i.e., adding new dimensions of complexity to antitrust suits." Pet. App. A12.

[24] "[W]e can never be absolutely certain that regulation has resulted in a 100 percent pass through; for all we know, [the direct purchaser] would have sought a rate increase but for the gas overcharge, and by forbearing to do so in effect absorbed part of the overcharge." Pet. App. A59. The Seventh Circuit found doubts on this score "too small to warrant" barring suit by indirect purchasers, *ibid.*, although this Court had pointed to just such doubts in *Hanover Shoe*. See 392 U.S. at 493 & n.9 ("the nearly insuperable difficulty of demonstrating that the particular plaintiff [a direct purchaser] could not or would not have raised his prices absent the overcharge").

here,[25] and they would also presumably seek to prove—if appropriate—that they did not pass on all of the overcharge. Indirect purchasers, generally more numerous than direct purchasers, may participate in the proceedings in various ways. If States choose to bring *parens patriae* actions, as here, natural persons may be represented by one or more state attorneys general, but they may also sue by class action or individually. Persons other than natural persons may not be represented by state attorneys general acting *parens patriae* and pre-

[25] We see no basis for preventing recovery of these lost profits by direct purchasers who are not permitted to recover the amount of the overcharge. Neither petitioners nor amici suggest any such limitation, the Tenth and Seventh Circuits appear to have assumed direct purchasers would still be able to sue for those lost profits, and permitting recovery by direct purchasers of their lost profits would seem consistent with this Court's analysis in *Hanover Shoe* of proof of damages where the purchaser cannot show a differential between the lawful price and the price unlawfully charged, 392 U.S. at 494. As Judge Feinberg perceived, permitting a pass-on defense amounts to requiring a direct purchaser to sue for lost profits, *Atlantic City Elec.*, 226 F. Supp. at 61-62, and some other principle would be required to deprive the direct purchaser of even lost profits damages. Proving the extent to which volume declined as a result of a price increase is likely to entail analysis of the same elasticities that troubled this Court in *Illinois Brick*, 431 U.S. at 742 ("a serious problem of measuring the relevant elasticities—the percentage change in the quantities of the passer's product demanded and supplied in response to a one percent change in price"). The difficulty of proving lost profits is, of course, one of the reasons for the indirect purchaser rule in the first place. See Point A.2, *supra*. The difficulty is less likely to arise if only the direct purchaser may recover the amount of the overcharge. Even if the direct purchaser is legally entitled to recover both the overcharge and lost profits from declining volume (assuming any overlap is eliminated), the difficulty of proving those lost profits appears generally to lead plaintiffs to conclude the game is not worth the candle, where the trebled amount of the overcharge is more readily available.

sumably would seek to recover either individually or through class actions.[26]

Proliferation of parties, and in particular of indirect purchaser parties, runs precisely the risks of insufficient incentive to sue and inadequate compensation of injured purchasers to which this Court referred in *Illinois Brick*, 431 U.S. at 745-747.[27] And if even the possi-

[26] In *Panhandle Eastern*, the court concluded that indirect purchasers other than residential consumers could not maintain damage actions, because the overcharge had not been passed through perfectly to them; the utility therefore was permitted to sue for the overcharge with respect to those consumers. In this case, we are aware of no basis for distinguishing between residential consumers and other consumers, or between natural person consumers and other consumers, with respect to passing on. We note that only the utilities in this case, as direct purchasers, have sued to recover the overcharge passed on to those customers who are not natural persons. It appears, therefore, that if the right to sue for the overcharge in this case belongs to indirect purchasers, the good news is that this litigation will not be complicated by the presence of *these* customers—but the bad news is that the defendants will escape liability for the overcharge passed on to customers who are not natural persons.

[27] We do not question the assertions of amici Forty-Six States concerning the power and efficacy of the *parens patriae* weapon or the capabilities of state attorneys general and their staffs. Forty-Six States Amici Br. 18-22. We disagree, however, with the argument advanced by petitioners, Br. 23-27, and amici National Conference of State Legislatures et al., Br. 5-21, that Section 4C of the Clayton Act, 15 U.S.C. 15c, authorizes state attorneys general to bring *parens patriae* actions on behalf of indirect purchasers who are natural persons. That argument is foreclosed by *Illinois Brick*.

In *Illinois Brick*, the United States as amicus curiae contended that Section 4 of the Clayton Act should be construed to allow indirect purchasers to recover illegal overcharges passed through to them by direct purchasers. The United States reasoned that (1) Section 4C incorporated the same definition of injury as Section 4; (2) Section 4C allows indirect purchasers to recover overcharges passed through by direct purchasers (as shown in the legislative history of Section 4C and the policy considerations underlying that

bility of recovery by indirect purchasers depends on proving perfect pass on, "[t]his additional uncertainty would

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provision); therefore (3) Section 4 should likewise be construed to authorize indirect purchaser suits. U.S. Amicus Br. at 14-15 & n.12. See 431 U.S. at 756-758 (Brennan, J., dissenting).

The Court agreed that Section 4C and Section 4 share the same definition of injury, but disagreed that Section 4 authorized indirect purchaser suits. 431 U.S. at 731 n.14. The Court accordingly rejected (albeit implicitly) the United States' submission that Section 4C should be construed to authorize indirect purchaser suits. 431 U.S. at 733-734 n.14. Although petitioners and amici concede, as they must, that Section 4 does not authorize indirect purchaser suits, Pet. Br. 23; National Conf. of State Legislatures et al., Amici Br. 6-7 & n.4, 17, their insistence that Section 4C nevertheless does authorize such suits simply disregards the Court's holding that Section 4C incorporated the definition of injury in Section 4. "Congress made clear, however, that [Section 4C] * * * simply created a new procedural device—*parens patriae* actions by States on behalf of their citizens—to enforce existing rights of recovery under § 4. The House Report * * * stated that the *parens patriae* provision 'creates no new substantive liability'; the relevant language of the newly enacted § 4C(a) of the Clayton Act tracks that of existing § 4, showing that it was intended only as 'an alternative means . . . for the vindication of existing substantive claims.' H.R. Rep. No. 94-99, *supra*, at 9 [(1975)]. 'The establishment of an alternative remedy does not increase any defendant's liability.' *Ibid.* * * * [Section 4C] did not create a right of recovery for consumers where one did not already exist [under Section 4]." 431 U.S. at 734 n.14.

In any event, the Court need not construe Section 4C in this case because the argument was neither pressed nor passed on by the courts below. Tellingly, petitioners do not contend that they pressed their view of Section 4C below, and amici's contention that they did ignores the court of appeals' correct observation that "[t]he parties have not argued that this law [Section 4C] eliminates the basic rule that only a direct purchaser may sue." Pet. App. A7 n.1. Amici quote the succeeding sentence for the proposition that the court of appeals decided the issue, National Conf. of State Legislatures, et al. Amici Br. 5 n.2, but the court of appeals' clearly "assume[d] that [Section 4C] comes into play when the individual consumers are the direct purchasers," *id.* at 6 n.3 (quoting Pet. App. A7 n.1), because neither petitioners nor amici suggested any contrary interpretation.

further reduce the incentive to sue" and "could seriously impair" the efficacy of treble damage actions. *Id.* at 745. The prospect of protracted litigation over which party may sue to recover the overcharge would make all parties less inclined to bring suit.

The special circumstances of regulation do not alter the analysis of incentives or compensation so as to justify permitting the attempt to prove a perfect pass through here. In response to the concern about increasing the number of parties to antitrust litigation, the Seventh Circuit hypothesized that "[t]he public utility commission may force the utility to pass on to the consumers any and all damages that the utility recovers, and if it does utilities will have no incentive to sue because they will have nothing to gain from suit." *Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Co.*, 852 F.2d at 895. But there are at least two problems with this hypothesis. First, it seems unlikely that a public utility commission would require dollar for dollar pass through to consumers of three times the amount of the overcharge the utility passed on, or dollar for dollar pass through of three times the amount of the utility's lost profits on volumes it did not sell to consumers (assuming the utility could recover that as well). Thus the utility would most likely have the not insignificant incentive of recovering twice the overcharge, and possibly the additional incentive of recovering three times its lost profits. Second, a public utility commission capable of requiring a utility to pass through its entire antitrust recovery to its customers would also seem capable of motivating a regulated utility to bring suit.[28]

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[28] A public utility commission might treat costs attributable to a suspected antitrust violation as costs imprudently incurred if the utility does not bring suit.

As to this case, the district court observed that "any recovery by the utilities * * * will be passed on in substantial part to the consumers." Pet. App. A36. We also note that the *parens patriae* statute does not require that amounts recovered be distributed to those

In sum, an exception to the indirect purchaser rule permitting suit by indirect purchasers who can prove complete pass through of an overcharge even though the direct purchaser is injured risks introducing nearly all the litigation complexity and diminution of incentives to sue which concerned this Court in *Illinois Brick*, without clearly offsetting benefits in terms of compensation or other relevant criteria.[29]

2. *A "100% Pass-Through" Exception Limited To Cases In Which Direct Purchasers Have A Written Legal Obligation To Pass Through Any Overcharge Should Not Be Created*

A less exacting exception to the indirect purchaser rule which would dispense with the need to prove perfect pass through of an overcharge presents a closer question under the *Illinois Brick* criteria. Indirect purchasers could be presumed as a matter of law to have borne 100% of the overcharge if the direct purchaser is subject to a written, legally binding obligation [30] to pass on the entire amount of an overcharge. In such cases, only the indirect purchasers would have the right to recover the overcharge from the antitrust violator. Although the presumption is

on whose behalf suit was brought, see 15 U.S.C. 15e, as this Court observed in *Illinois Brick*, 431 U.S. at 747 n.31.

[29] If such an exception were justified, there would also be a strong case for an exception permitting suit where the pass on is less than 100%, but the amount can easily be proved. It is not obvious that it is intrinsically more difficult to prove a 95% pass through than to prove a 100% pass through, and the differential incentive effects may not be significant. Once the principle that a direct purchaser who is injured may sue for the entire overcharge is abandoned and indirect purchasers permitted to sue if they can prove some particular portion of the overcharge was passed on, there is no obvious stopping point short of complete abandonment of the indirect purchaser rule.

[30] Such an obligation could arise in many ways, including statute, regulation, contract, and filed tariff. The presumption, of course, would not apply if the direct purchaser is excused from the legally binding obligation by some official legislative or regulatory action or by other written modification of the obligation.

bound to be incorrect in some cases, it is likely to be correct, or nearly so, in the vast majority of cases.

Reliance on this presumption would avoid the complex task of proving the extent of pass through, substituting for it the far more judicially manageable task of proving the meaning of writings. Moreover, the meaning of the writings may often be sufficiently clear to remove uncertainty about, and litigation over, which parties have the right to sue to recover the overcharge. Thus, the efficacy of private antitrust enforcement would not suffer to the extent it would were proof of the extent of pass on necessary. Whatever benefits might result from permitting indirect purchaser suits in these limited circumstances would be available without complex and protracted litigation over who may bring suit.

The benefits of such an exception, however, are neither obvious nor compelling, and there remain costs to be considered. To be sure, permitting indirect purchasers to bring suit where the overcharge has been passed on to them may increase the extent to which these indirect purchasers are compensated for their injuries.[31] But the Court was plainly aware of this possibility when it barred suit by indirect purchasers in *Illinois Brick*. See 431 U.S. at 746-747. Moreover, in the regulatory context, pass through of portions of the direct purchaser's antitrust recovery may compensate indirect purchasers at least as well. See p. 25 & note 28, *supra*. And while indirect purchasers might have adequate incentive to sue despite their small individual stakes,[32] we have already noted

[31] Because the exception considered here does not depend on proof of actual pass on, direct purchasers would not be compensated for the portion of the overcharge they absorbed. To some, this prospect may be no more troubling than undercompensation of indirect purchasers as a result of the indirect purchaser rule (although perhaps harder to rationalize), but the failure to compensate injured direct purchasers fully does counterbalance the increased compensation of indirect purchasers under the rule here considered.

[32] Petitioners assert that the *parens patriae* mechanism remedies the Court's concern about the consequences of the small stake of the individual indirect purchaser for antitrust enforcement, Br. 20,

that the direct purchaser's incentive to sue is unlikely to vanish even if regulation requires pass through of the recovered overcharge.[33]

The costs of such an exception could be significant. Even if there is no increase in complexity related to proving a legal obligation to pass on the entire overcharge, there remain additional sources of litigation complexity. First, there is the increase in the number and diversity of status of plaintiffs, which would be no less under a rule which turns on legal obligation to pass on than under a rule which turns on proof of pass on. Second, the direct purchaser barred from recovering the overcharge presumably would, as under the other proposed exception, attempt to prove lost profits, a complex undertaking. Third, there may be substantial complexities associated with proving the individual damages of indirect purchasers.[34]

This proposed exception to the indirect purchaser rule also does not clearly single out circumstances that justify the exception from other, related circumstances. Indeed, the Seventh Circuit refused to say whether the exception it carved out would apply to other cost-plus contracts as

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but the *parens patriae* mechanism cannot remedy that concern with respect to indirect purchasers who are not natural persons and whom state attorneys general may not represent *parens patriae*.

[33] Parties to contracts which pass through overcharges are free to provide for whatever treatment of the direct purchaser's antitrust recoveries they desire. They therefore may structure their contracts to provide adequate incentive for the direct purchaser to sue and compensation for the indirect purchaser.

[34] As petitioners correctly observe, Br. 14 n.9, "aggregate" proof of damages may obviate this problem in *parens patriae* actions. However, only natural persons may be represented by state attorneys general *parens patriae*, and an alternative approach to damages may be necessary for other indirect purchasers. Moreover, the problem of proof may be difficult if the direct purchaser, although obligated to pass on the entire overcharge, is not obligated to pass on to each indirect purchaser in proportion to the amount purchased. The basis on which individual damages would then be determined is unclear.

well as to regulated contracts and cost-plus requirements contracts. Pet. App. A59. Moreover, as we have noted (note 29, *supra*), most of petitioners' arguments would apply with only marginally reduced force where regulation requires a pass through of any fixed percentage.

The issue before this Court is not whether it should abandon the indirect purchaser rule. It is whether the circumstances petitioners identify present a sufficiently compelling justification for carving out an exception to the principles of antitrust damage recovery this Court has endorsed and consistently followed since 1906. We submit that the justifications offered are not sufficiently compelling to embark on such an enterprise.

CONCLUSION

The judgment of the Tenth Circuit should be affirmed.

Respectfully submitted.

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No. 88-2109

IN THE
Supreme Court of the United States

OCTOBER TERM, 1989

THE STATES OF KANSAS and MISSOURI,
AS *Parens Patriae*,
Petitioners,
v.

THE KANSAS POWER & LIGHT COMPANY and
UTILICORP UNITED, INC.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

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**BRIEF OF THE
NATIONAL CONFERENCE OF STATE LEGISLATURES,
INTERNATIONAL CITY MANAGEMENT ASSOCIATION,
COUNCIL OF STATE GOVERNMENTS,
NATIONAL ASSOCIATION OF COUNTIES,
NATIONAL GOVERNORS' ASSOCIATION,
NATIONAL LEAGUE OF CITIES, AND
U.S. CONFERENCE OF MAYORS
AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS**

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QUESTION PRESENTED

Amici will address the following question:

Whether, under Section 4C of the Clayton Act, enacted by Congress in the Hart-Scott-Rodino Antitrust Improvements Act of 1976, State Attorneys General may bring actions as *parens patriae* on behalf of indirect purchasers who have been injured as a result of a violation of the Sherman Act.

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INTEREST OF THE *AMICI CURIAE*

The *amici*, organizations whose members include state, county, and municipal governments and officials throughout the United States, have a compelling interest in legal

issues that affect state and local governments. This case concerns the right of State Attorneys General under Section 4C of the Clayton Act—enacted into law by the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 15c-h—in their capacity as *parens patriae*, to recover damages on behalf of their natural citizens who have been injured by violations of the Sherman Antitrust Act, 15 U.S.C. §§ 1-7.

Pursuant to Section 4C, Kansas and Missouri asserted claims on behalf of residential consumers of natural gas. The gas was purchased from public utilities that had, pursuant to law, passed on to the consumers the price increases occasioned by a price-fixing conspiracy on the part of the utilities' suppliers. The court of appeals held that the States' *parens patriae* claims must be dismissed because of the holding in *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), that, with limited exceptions, indirect purchasers cannot recover damages under Section 4 of the Clayton Act, 15 U.S.C. § 15, for price-fixing violations.

Amici's concern is with the failure of the courts below to give effect to the authority conferred upon the State Attorneys General by Section 4C of the Clayton Act. In that provision, Congress authorized the State Attorneys General in their *parens patriae* capacity to recover damages inflicted upon their natural citizens by violations of the Sherman Act without regard to whether their citizens were indirect or direct purchasers. Section 4C creates a right of action separate and apart from Section 4 of the Clayton Act, the statutory provision interpreted in *Illinois Brick* and *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968).

Just last Term, in *California v. ARC America Corp.*, 109 S.Ct. 1661 (1989), the Court held there is a presumption against federal preemption of state antitrust law. The present case presents a corollary to that principle: when Congress expressly recognizes the right of a State

Attorney General to bring a *parens patriae* action, that right should be given full effect. In *ARC America*, the Court held that the bar on indirect purchaser suits announced in *Illinois Brick* did not preempt state laws permitting recovery of antitrust damages by indirect purchasers. *Amici* are concerned that the failure to uphold the authority that Congress expressly gave to the State Attorneys General in Section 4C of the Clayton Act will frustrate state antitrust efforts no less than preemption of the State's own laws.

Amici submit that the decision below is wrong. Because this Court's decision will have a direct effect on matters of prime importance to *amici* and their members, *amici* submit this brief to assist the Court in its resolution of the case.[1]

STATEMENT

Amici adopt the statement of the case of the petitioners.

SUMMARY OF ARGUMENT

The claims dismissed below were brought by State Attorneys General as *parens patriae* under Section 4C of the Clayton Act on behalf of consumers who are indirect purchasers ("indirect consumer purchasers") of natural gas that was the subject of a price-fixing conspiracy. The court of appeals dismissed on the authority of this Court's decision in *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), which addressed the right of indirect purchasers to sue under Section 4. In its only reference to Section 4C, the court of appeals stated its assumption that Section 4C "comes into play when the individual consumers are the direct purchasers." Pet. App. A7 n.1. This assumption was error. The cause of action created by Section 4C is distinct from a cause of action under Section 4, and this Court has never determined the right of State Attor-

[1] The parties' letters of consent, pursuant to Rule 37 of the Rules of the Court, have been filed with the Clerk.

neys General under Section 4C of the Clayton Act to sue as *parens patriae* on behalf of indirect consumers for injury resulting from violations of the Sherman Act.

Section 4C of the Clayton Act was enacted in 1976 as part of the Hart-Scott-Rodino Antitrust Improvements Act of 1976. It authorizes suits on behalf of natural persons by State Attorneys General as *parens patriae*. The structure and language of Section 4C and the statute's legislative history make clear that Congress created a new cause of action to remedy perceived procedural and technical difficulties in providing compensation to consumers, including indirect consumer purchasers, for injuries suffered as a result of violations of the Sherman Act. Section 4C did not enlarge the scope of the violations defined by the Sherman Act, but rather provided a new remedy—separate and distinct from Section 4—to ensure the right of the ultimate consumer, whether a direct or indirect purchaser, to be compensated for damages resulting from such violations.

Congress's intent in enacting Section 4C—to provide a remedy to consumer purchasers, whether direct or indirect—would be extinguished if this Court's limitations in *Illinois Brick* on the right of indirect purchasers to bring suit under Section 4 of the Clayton Act is engrafted onto Section 4C. Section 4C's authorization of *parens patriae* actions to be brought by State Attorneys General reflects Congress's judgment of the balance to be struck in this type of action among the distinct policies of victim compensation, effective antitrust enforcement, and judicial economy. This Court, in *Illinois Brick* reached a different judgment when confronted with an indirect purchaser suit brought under Section 4 of the Clayton Act, which does not contain a *parens patriae* provision or other features of Section 4C pertinent to indirect purchasers. The Court should now give full effect to Congress's intent in enacting Section 4C by upholding the right of State Attorneys General pursuant to Section 4C of the Clayton Act

to bring *parens patriae* actions on behalf of indirect consumers for violations of the Sherman Act.

ARGUMENT

SECTION 4C OF THE CLAYTON ACT AUTHORIZES STATE ATTORNEYS GENERAL TO BRING *PARENS PATRIAE* ACTIONS ON BEHALF OF INDIRECT PURCHASERS.

A. This Court Has Not Decided Whether A *Parens Patriae* Action On Behalf Of Indirect Consumer Purchasers May Be Brought Pursuant To Section 4C Of The Clayton Act.

This case presents the question whether a State Attorney General as *parens patriae* may seek damages for violations of the Sherman Act pursuant to Section 4C—not Section 4—of the Clayton Act on behalf of consumers who are indirect purchasers.[2] This question of statutory construction has not previously been reviewed by this Court, and we contend that none of this Court's prior antitrust decisions is dispositive, including notably *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968), and *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977). The decisions of the Seventh Circuit in *State of*

[2] The question as we have framed it is properly before the Court because it is fairly comprised within the question presented and was decided by the court below. The complaints initiating the actions before the Court were filed by Kansas and Missouri as *parens patriae* and were specifically brought pursuant to Section 4C of the Clayton Act. See Missouri's Second Amended Complaint, ¶ 2; Kansas's First Amended Complaint, opening paragraph. Moreover, the question presented by petitioners regarding the right of State Attorneys General to sue *parens patriae* necessarily references Section 4C of the Clayton Act because that is the only section expressly permitting such suits. Indeed, the petition for writ of certiorari argues (at page 14) that the decision below frustrates the purpose of Section 4C. Finally, the Tenth Circuit "assumed" that States did not have a right to sue under Section 4C as *parens patriae* on behalf of indirect purchasers. Pet. App. A7 n.1.

Illinois ex rel. Hartigan v. Panhandle Eastern Pipe Line Corp., 852 F.2d 891 (7th Cir.) (en banc), cert. denied, 109 S.Ct. 543 (1988), and the Tenth Circuit below are in error to the extent that both treat the authority of a State Attorney General to bring a *parens patriae* suit on behalf of indirect consumer purchasers as turning on whether such a suit falls within an exception to the general ban on indirect purchaser suits under Section 4 of the Clayton Act set forth in *Illinois Brick*.[3]

Neither *Illinois Brick* nor its predecessor, *Hanover Shoe*, purported to construe Section 4C. *Hanover Shoe* was decided eight years before Section 4C was enacted. And *Illinois Brick*, decided the year after Section 4C became law, did not involve the right of a State Attorney General to sue as *parens patriae* under Section 4C.[4] Indeed, it could not have done so because the State of Illinois, the plaintiff in that case, did not sue as *parens patriae* on behalf of injured consumers. It sued, rather, on behalf of itself and other governmental entities who were themselves indirect purchasers of concrete blocks used in state building projects.[5]

The Hart-Scott-Rodino Antitrust Improvements Act was enacted eighty-six years after the Sherman Act, and

[3] As indicated, the court below assumed that Section 4C "comes into play when the individual consumers are the direct purchasers." Pet. App. A7 n.1. The district court opinion in *State of New York v. Dairylea Co-op. Inc.*, 570 F. Supp. 1213, 1215-16 (S.D.N.Y. 1983), also treats Section 4C as applying only to consumers who are direct purchasers.

[4] The Court's opinion in *Illinois Brick* does include a discussion of the legislative history of the Act, but solely in the context of determining the implications of that history for a proper construction of Section 4. 431 U.S. at 733 n.14, 747 n.31.

[5] Even if the State had wanted to sue as *parens patriae*, it could not have done so because Section 4C of the Act did not apply to suits filed prior to enactment. See Pub. L. No. 94-435, § 304, 90 Stat. 1396. Moreover, the claimants in that suit were not natural persons as is required by Section 4C.

sixty-two years after the Clayton Act, which contains Section 4. It was enacted over vigorous opposition and after extensive debate in both Houses. A plain reading of the Act, as well as its legislative history, make clear that Section 4C has a structure and purpose distinct from Section 4 and must be interpreted in light of its own language, structure, purpose, and legislative history—not that of Section 4.

B. The Language Of The Hart-Scott-Rodino Act Specifically Created A New Remedy, *Parens Patriae* Suits, On Behalf Of Consumers, Whether Direct Or Indirect Purchasers.

As is true in every case involving statutory construction, the analysis must begin with the language employed by Congress, *Schreiber v. Burlington Northern, Inc.*, 472 U.S. 1, 5 (1985); *Reiter v. Sonotone Corp.*, 442 U.S. 330, 337 (1979). Section 4C of the Clayton Act, 15 U.S.C. § 15c, provides in pertinent part:

> Any attorney general of a State may bring a civil action in the name of such State, as parens patriae on behalf of natural persons residing in such State, in any district court of the United States having jurisdiction of the defendant, to secure monetary relief as provided in this section for injury sustained by such natural persons to their property by reason of any violation of the Sherman Act.

In enacting Section 4C, Congress intended to create a new cause of action for the specific purpose of allowing consumers, including indirect purchasers, to be compensated for violations of the Sherman Act.[6] Congress also

[6] See discussion in Part C *infra*. That Section 4C actions are separate from Section 4 actions is confirmed by the language of Section 4B, 15 U.S.C. § 15b, as amended by the Hart-Scott-Rodino Act, which provides that "[a]ny action to enforce any cause of action under sections 15, 15a, or 15c of this title shall be forever barred unless commenced within four years after the cause of action accrued." Section 4 appears as Section 15 in the U.S. Code, and Section 4C appears as Section 15c.

provided distinctive features for this new cause of action to alleviate problems that had impeded such relief in the past in actions brought under Section 4. The *parens patriae* form, for example, aggregates consumer claims, thereby providing an incentive for enforcement of the antitrust laws. This incentive is enhanced by placing control of such actions solely in the hands of a responsible law enforcement official.

Section 4C further provides that in awarding monetary relief the court "shall exclude . . . any amount of monetary relief which (A) duplicates amounts which have been awarded for the same injury, or (B) which is properly allocable to . . . (ii) any business entity." This language and structure leave no doubt that Congress intended to authorize suits on behalf of indirect purchasers. Only if both direct and indirect purchasers may bring suit for the same price-fixing violation will the possibility arise of a duplicative damage award for the same injury or of damages properly allocable to a business entity.

It is a fundamental article of statutory construction that a statute should be interpreted to give effect to each of its words. *Mountain States Telephone & Telegraph Co. v. Pueblo of Santa Ana*, 472 U.S. 237, 249 (1985); *Reiter v. Sonotone Corp.*, 442 U.S. at 339. The exclusionary language of Section 4C can have no effect except in the context of a suit brought on behalf of indirect purchasers. Thus, the statute should be construed to include both direct and indirect purchasers within the class of natural persons on whose behalf a *parens patriae* action may be brought.

Indeed, if Section 4C were construed to apply only to direct consumer purchasers, then many, perhaps most, antitrust violators would be beyond its reach.[7] This is so

[7] This is not true for Section 4 of the Clayton Act, which allows any "person" (which has been construed to include a corporation or other business entity) to bring suit. Thus, even though *Illinois*

because, under Section 4C, a *parens patriae* suit may only be brought on behalf of natural persons; and in most distribution chains in which a Sherman Act violation occurs, there will be no "natural person" purchasing directly from the violator.

Thus, if Section 4C is construed to exclude indirect consumer purchasers, then whenever a Sherman Act violation occurred more than one level in the distribution chain above the consumer, the Attorney General could not bring a Section 4C action. Nothing in the language of Section 4C indicates a congressional intent to immunize antitrust violators who do not trade directly with consumers from such actions.[8] Such a construction would frustrate the manifest intent of Congress to enable State Attorneys General to vindicate consumers' interests in goods flowing through a market unimpeded by price-fixing (and other Sherman Act violations), wherever in the chain of distribution these violations might occur. For the Act to achieve its purpose, it must be construed to reach indirect consumer purchasers.

Brick bars indirect purchasers from bringing suit under Section 4, the effect is not to insulate antitrust violations from suit under Section 4. Some entity—be it a natural person or a business entity—will have purchased directly from the antitrust violator and will have standing to sue.

[8] Section 4C does contain language similar to Section 4 regarding the injury requirement. Thus, Section 4C refers to "injury sustained by such natural persons to their property by reason of any violations of the Sherman Act," and Section 4 refers to "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws." This similarity cannot mean, however, that the interpretation given by this Court in *Illinois Brick* to "injury" in Section 4 should be grafted onto Section 4C. The meaning given to "injury" in Section 4C by Congress must be determined by construing that term as it is used in Section 4C itself. See *Dole v. United Steelworkers of America*, No. 88-1434 (Feb. 21, 1990), slip op. 8 (in construing a statute, court must look to the entire law and its object and policy).

C. The Legislative History Of The Hart-Scott-Rodino Act Confirms Congress's Intent To Authorize *Parens Patriae* Suits On Behalf Of Indirect Purchasers.

The legislative history of the Hart-Scott-Rodino Act confirms Congress's intent to authorize *parens patriae* suits on behalf of individual consumers, whether they are direct or indirect purchasers, who suffer injury as a result of violations of the Sherman Act. The legislative reports and the floor debate demonstrate beyond question that Congress considered the problems that may be associated with indirect purchaser suits, and designed Section 4C to address these problems, to compensate injured consumers, and to deter antitrust violations.

1. *The House and Senate Reports both show an intent to authorize* parens patriae *suits on behalf of indirect purchasers.*

Both the House and Senate Reports evidence Congress's intention that the *parens patriae* suits that were specifically authorized in behalf of individual consumers include indirect, as well as direct, purchasers. The House Report sets out the purpose of the *parens patriae* provision in broad and general terms—to "permit State attorneys general to recover monetary damages on behalf of State residents injured by violations of the antitrust laws." H.R. Rep. No. 499, 94th Cong., 1st Sess. 3, reprinted in 1976 U.S. Code Cong. & Ad. News at 2572. There is no suggestion that Congress intended to limit this remedy to direct purchasers. The Report goes on to discuss the problem of price-fixing in particular, which it states creates an economic burden that "is borne in large measure by the consumer in the form of higher prices for his goods and services. . . . [P]ractices [such as price-fixing] usually result in higher prices for the consumer, regardless of the level in the chain of distribution at which the violation occurs." *Ibid.*, reprinted in 1976 U.S. Code Cong. & Ad. News at 2573. Clearly, this was a bill intended to address consumer interests.

The House Report specifically addresses whether a consumer who is an indirect purchaser has a remedy under Section 4C: "Under section 4 of the Clayton Act, any person, including *any* consumer, who can prove he was injured by price-fixing or any other antitrust violation, has a cause of action." House Report at 6, reprinted in 1976 U.S. Code Cong. & Ad. News. at 2575 (emphasis added). A footnote to that sentence notes that some courts had initially read *Hanover Shoe* to limit standing to sue to the direct purchaser only, but "[m]ore recently lower courts have recognized the pro-enforcement thrust of *Hanover Shoe* and have held that plaintiffs at lower levels of the chain of distribution may attempt to prove that illegal overcharges were in fact passed on to them." House Report at 6 n.4, reprinted in U.S. Code Cong. & Ad. News at 2576. The Report cites in particular *In Re Western Liquid Asphalt Cases*, 487 F.2d 191 (9th Cir. 1973), cert. denied *sub nom. Standard Oil Co. of California v. Alaska*, 415 U.S. 919 (1974), a case that would have allowed indirect purchasers to recover.[9] *Ibid.*

Thus, it is apparent that when Congress enacted Section 4C, it believed that indirect consumer purchasers had a cause of action under Section 4, but was concerned that the small damage suffered by any individual consumer would chill the incentive to bring suit under Section 4. House Report at 6, reprinted in U.S. Code Cong. & Ad. News at 2575; cf. *Illinois Brick*, 431 U.S. at 747 n.31. The *parens patriae* provision was Congress's carefully crafted legislative response to this concern. It was intended to overcome this problem for all consumers,

[9] The House Report reference to Section 4 of the Clayton Act reflects the fact the bill on which the report was issued, H.R. 8532, created a cause of action under Section 4 of the Clayton Act. The bill in pertinent part provided that "[a]ny State attorney general may bring a civil action . . . under section 4 of this Act." The statute ultimately enacted, however, is not premised on Section 4 of the Clayton Act, but provides a separate cause of action. See note 14, *infra*.

whether direct or indirect purchasers. The House Report explicitly states that "[w]here, however, *wholesalers and retailers have passed on all or most of the cost of a violation to the consumer*, or where the violation itself occurred at the retail level (thus subjecting the consumer to the major impact of the violation), adequate enforcement mechanisms simply do not exist." House Report at 7-8, reprinted in 1976 U.S. Code Cong. & Ad. News at 2577 (emphasis supplied).

The Senate Report, too, demonstrates the clear intent to provide a remedy for consumers who are indirect purchasers. The purpose of the *parens patriae* provision is "to permit State attorneys general to recover damages for violations of the Sherman Act to secure redress for damage done to natural persons (consumers) residing in their State." S. Rep. No. 803, 94th Cong., 2d Sess. 39 (1976) (footnote call omitted). The Report also states that Section 4C "creates a new statutory cause of action for States." *Id.* at 42.[10] It further explains that "Section 4C is intended to assure that consumers are not precluded from the opportunity of proving the amount of their damage and to avoid problems with respect to manageability, standing, privity, target area, remoteness, and the like." *Ibid.*[11] Later in the Report, the intent to include indirect purchasers is again indicated: the statutory language was intended "to avoid the previously referred to problems associated with such concepts as remoteness, target area, privity of contract, *passing on, etc.*" *Id.* at 45 (emphasis added).

[10] The Senate bill, which in this respect was enacted into law, does not premise the cause of action on Section 4 of the Clayton Act, as did the House bill. See note 14, *infra*.

[11] This statement is particularly germane to the issue before this Court because, before *Illinois Brick*, the *Hanover Shoe* doctrine was often conceived to be one of standing. See *Illinois Brick*, 431 U.S. at 732 n.14.

It was so clearly the intent of the drafters of Section 4C to permit suit on behalf of indirect consumer purchasers that they drafted other components of the bill to ensure that this result would not create inconsistencies. Thus, the Senate Judiciary Committee rejected efforts to delete the treble damage component from *parens patriae* actions under Section 4C on the ground that this would lead to inequitable results: if *parens patriae* actions were limited to only single damages, and if, for example, direct purchasers passed on one-half of an illegal overcharge to a consumer and absorbed the other half, then the direct purchasers "could collect treble damages for the one-half they absorbed but the consumer could collect only single damages for the passed on one-half." Senate Report at 45.

The Senate Judiciary Committee was also concerned with the problem of double recovery, which could only occur if both direct and indirect purchasers were allowed to sue. Accordingly, the Senate Report explains (at page 44-45) (emphasis added) that Section 4C

> contains a proviso to assure that defendants are not subject to duplicative liability, particularly in a chain-of-distribution situation where it is claimed that middlemen absorbed all or part of the illegal overcharge. . . . *As between competing claimants within the chain of distribution, however, including consumers*, the Section 4C(a)(1) proviso is intended to assure that the monetary relief is properly allocated.

Finally, the Report states it was the Committee's intention to codify *In re Western Liquid Asphalt Cases*, 487 F.2d 191 (9th Cir. 1973), cert. denied *sub nom. Standard Oil Co. of California v. Alaska*, 415 U.S. 919 (1974), a case which would have allowed the offensive use of a pass-on theory. See *Illinois Brick*, 431 U.S. at 730 n.11. The Senate Report reprints a discussion from *In re Western Liquid Asphalt* concerning various procedural devices to avoid double recovery. Senate Report at 44.

The Senate and House Reports were available to both Houses before they finally approved the Hart-Scott-Rodino Act. Accordingly, these two Reports are entitled to significant weight as evidence of congressional intent. See *National Ass'n of Greeting Card Publishers v. United States Postal Service*, 462 U.S. 810, 832 n.28 (1983). Both Reports demonstrate beyond doubt that a basic intention of the drafters was to ensure that suits on behalf of indirect consumer purchasers could be brought under Section 4C.

2. The record of the floor debates in both the Senate and the House indicates that Congress understood Section 4C to authorize* parens patriae *suits on behalf of indirect purchasers.

On March 18, 1976, the House of Representatives debated and passed H.R. 8532, entitled the "Antitrust Parens Patriae Act." This was the House version of the bill that, after amendment by the Senate, was finally enacted into law as the Hart-Scott-Rodino Act. The record of the debate fully supports the view that Congress intended to create a cause of action that would provide a remedy for indirect purchasers.

The right of indirect purchasers to recover under the bill was not disputed, even by the opponents of the bill. They were concerned, however, that indirect purchasers be allowed to recover only for that portion of the illegal overcharge actually passed on to them by the direct purchaser. Thus, Congressman Wiggins, a member of the Judiciary Committee that drafted the bill (which he opposed), stated: "This whole problem of pass-through is a technical one; but I am of the opinion that the bill does not relieve the plaintiff of the duty of proving that damages have been passed through to individual claimants." 122 Cong. Rec. 7031 (1976). Congressman Wiggins also questioned the impact a *parens patriae* action would have on other innocent purchasers who were further up the chain of distribution. He asked: "[I]f an attorney general brings a parens patriae case on behalf of 'consumers,' must every other natural person in the chain of distribution 'opt out' in order to protect his own rights to bring an independent treble damage action?" *Ibid.* If only the direct purchaser were covered by the Act, this question would be without meaning.

Congressman Symms, also an opponent of the bill, cited *Hanover Shoe* as support for his argument that "[a]rriving at an estimate of damages which were actually suffered by the consumer will be impossible." 122 Cong. Rec. 7035 (1976). This reference to the difficulty of tracing an illegal overcharge through the chain of distribution is simply another manifestation of a shared understanding among both the proponents and opponents of the bill that indirect consumer purchasers were beneficiaries of the bill.

On September 16, 1976, the House, after debate, passed the Hart-Scott-Rodino Antitrust Improvements Act of 1976, which was the Senate-passed version of the earlier House bill. Congressman Rodino, in his extensive remarks regarding the bill, explicitly discussed the indirect purchaser issue. Congressman Rodino stated that "assuming the State attorney general proves a violation, and proves that an overcharge was 'passed on' to the consumers, injuring them 'in their property'; that is, their pocketbooks —recoveries are authorized by the compromise bill whether or not the consumers purchased directly from the price fixer, or indirectly, from intermediaries, retailers, or their middlemen." 122 Cong. Rec. 30878 (1976). In even stronger terms, Congressman Rodino remarked that "the manufacturer invariably sells through wholesalers and retailers—grocery stores, drug stores, and the like—and if the intervening presence of such a middleman is to prevent recovery, the bill will be utterly meaningless." *Ibid.* This language is absolutely clear, and it is consistent with the statute itself and the remainder of the legislative history. Moreover, it expresses the views of a chief

sponsor of the bill. As such, it is excellent evidence of congressional intent. *North Haven Board of Education v. Bell*, 456 U.S. 512, 526-27 (1982), and cases cited.

The debates in the Senate are to the same effect. Senator Hart, one of the principal drafters of the Senate bill (S.1284) introduced the bill to the Senate on May 25, 1976, with extensive remarks.[12] There he summarized the elements that a State Attorney General has the burden of proving:

> First, the defendants violated the Sherman Act;
>
> Second, that consumers were injured by the violation *or that some of the overcharge was passed on to them*; and
>
> Third, the approximate amount of such damage.

122 Cong. Rec. 15311 (emphasis added). Again, as a sponsor of the bill, Senator Hart's remarks are particularly probative. To Senator Hart it was clear that injury to indirect purchasers could be remedied under the bill.

Indeed, Senator Bellmon, an opponent of the bill, used this very feature as a means to attack the bill's necessity. "[M]ost of the defendants who are sued in consumer actions," he argued, "are businesses that deal with other business enterprises before their products ever reach consumers." 122 Cong. Rec. 15323 (1976). From this, Senator Bellmon concluded that whenever an antitrust violation occurs, a direct purchaser will be present and ready to bring a "well-financed and competent" suit, and that therefore the "specter of a violator retaining huge illegal profits" absent the *parens patriae* procedure is

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[12] Senator Hart stated that Title IV, the *parens patriae* section of the bill, "would create a new statutory cause of action whereby the State attorney general could sue for treble damages and other relief on behalf of consumers." 122 Cong. Rec. 15311 (1976).

mythical."[13] *Ibid.* Senator Bellmon's unsuccessful opposition demonstrates how thoroughly recognition that the bill would create a cause of action on behalf of indirect purchasers permeated the debate.[14]

D. This Court's Treatment Of The Legislative History Of The Hart-Scott-Rodino Act In *Illinois Brick* Is Not Inconsistent With The Foregoing Argument And Has No Bearing On Whether An Action On Behalf Of An Indirect Purchaser May Be Brought Under Section 4C.

The Court's discussion in *Illinois Brick* of the legislative history of Section 4C is limited to two footnotes. 431 U.S. at 733 n.14, 747 n.31. In no way is that discussion inconsistent with our contention that Section 4C provides a cause of action for indirect purchasers. Addressing itself to an argument made in the dissent, the Court discussed only whether, under *Hanover Shoe*, the pass-on rule under Section 4 of the Clayton Act should be limited to defensive use. As such, the Court's discussion has no relevance to the issue presently before this Court.

In his dissent in *Illinois Brick*, Justice Brennan concluded that "Congress' interpretation of § 4 in enacting the *parens patriae* provision should resolve [the ques-

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[13] Senator Bellmon referred to the *Hanover Shoe* decision to bolster his argument that the direct purchaser would be an effective plaintiff, even where it had "passed on" the price increase to consumers. 122 Cong. Rec. 15325, 15326 (1976).

[14] For further example, Senator Bellmon referred to the "impracticability of trying a lawsuit to determine whether the financial effects of an antitrust violation have been passed on to an individual consumer." 122 Cong. Rec. 15326 (1976). Senator Bellmon inserted into the record an excerpt from a letter by Professor (now Judge) Posner opposing the bill that also discussed the difficulty of tracing the economic ramifications of an antitrust violation throughout a state's economy. *Ibid.* It is clear that Congress, in enacting this legislation, deemed none of these problems sufficient to bar the creation of a cause of action for indirect purchasers.

tion whether indirect purchasers could recover for damages passed on to them] in favor of their authority to sue." 431 U.S. at 758. The Court disagreed, on the grounds that these interpretive statements were made after the enactment of the Clayton Act and as such could not be used to show the intent of a prior Congress. 431 U.S. at 733 n.14. Nevertheless, the Court plainly agreed with Justice Brennan that the legislative history evidenced Congress's view at the time it enacted Section 4C that indirect purchasers could bring suit under Section 4. *Ibid.* As noted, *Illinois Brick* was not a *parens patriae* action under Section 4C. The Court's decision not to rely on Congress's interpretation in 1976 of Section 4, which was enacted in 1914, is neither remarkable (see *Consumer Product Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 117-18 (1980), and cases cited) nor relevant to whether Section 4C creates a cause of action designed to remedy injury suffered by indirect purchasers.

Congress's intent in enacting Section 4C in 1976 is to be determined by the language of the statute, and, to the extent there is any question of interpretation, the legislative history of that statute. When it enacted a new cause of action to remedy consumer injury, Congress held an interpretation of Section 4 that this Court subsequently rejected in *Illinois Brick*. But this Court's construction of Section 4 in *Illinois Brick*, after the enactment of Section 4C, cannot have any bearing on what Congress intended in enacting Section 4C.[14] As demonstrated above, Congress intended to create a new cause of action that would provide a remedy to consumers—whether direct or indirect purchasers—injured by violations of the Sherman Act. That intent should be given full effect by the Court.

[14] This Court's statement in *Illinois Brick* that Congress intended Section 4C to be solely a procedural device to permit consumers injured within the meaning of Section 4 to bring suit (see 431 U.S. at 733 n.14) is not supported by the statute or its legislative history. The Court relied upon the House Report as support for the statement that Section 4C(a) "tracks" Section 4. The House Report quoted, however, concerned House Bill 8532, which was substantially revised before enactment. Of critical importance is that Section 4C(a) of the House bill did track Section 4 of the Clayton Act. It provided: "[a]ny State attorney general may bring a civil action . . . under Section 4 of this Act." Section 4C as enacted does not refer to or rely upon Section 4. A summary of the differences between the Senate and House passed bills and the bill ultimately passed by both Houses (the Byrd motion) appears at 122 Cong. Rec. 29151 (1976). With respect to this point, the summary states as follows:

DIFFERENCES BETWEEN SENATE AND HOUSE PASSED BILLS AND BYRD MOTION

III. PARENS PATRIAE

A. Major Issues

Subject	Senate	House	Provision in Byrd motion
1. Separate cause of action.	Senate bill creates a separate cause of action in the name of the State.	House bill authorizes parens patriae action under section 4 of Clayton Act by State attorneys general.	Senate

Thus, it is clear that the bill enacted created a separate and independent cause of action. The views of those in the House who sought an arguably more restricted statute cannot control the interpretation of the bill actually passed. See *Hardin v. Kentucky Utilities Co.*, 390 U.S. 1, 11 (1968).

E. Section 4C Reflects Congress's Judgment On The Proper Balance Among Enforcement, Compensation, And Judicial Efficiency.

In enacting Section 4C, Congress was well aware of the family of concerns that would be expressed a year later by this Court in *Illinois Brick* regarding the inad-

visability of permitting antitrust actions under Section 4 by indirect purchasers. See, *e.g.*, Appendix 9 to Senate Report Part II—Minority Views (March 3, 1976, letter of Professor Posner).

In *Hanover Shoe*, this Court indicated its concern with the problems of providing an adequate incentive for injured parties to sue for antitrust violations, with the possibility of duplicative recoveries, and with the difficulty of ascertaining the amount of any pass-on of unlawful overcharges. As the statutory language and legislative history make clear, Congress in Section 4C created a new cause of action to deal with these concerns.

Section 4C provides an adequate incentive to sue where a large number of consumers have each suffered a small injury by creating a remedy that aggregates consumers' claims. House Report at 6, reprinted in U.S. Code & Ad. News at 2575. To ensure that these claims would be handled responsibly and to enhance the incentive to sue, *parens patriae* actions may be brought only by the Attorney General of a State.

Section 4C provides a specific mechanism to avoid duplicative damages that may result when both direct and indirect purchasers sue. A court in awarding damages under Section 4C ~~must exclude~~ any damages awarded to other parties for the same injury.

Finally, Section 4C requires the trial court to apportion damages. Recognizing that this requirement presented a difficult task for both the plaintiff and the courts, Congress nonetheless specifically provided that a court in making an award of damages under Section 4C must exclude damages that should be apportioned to any business entity.

That Congress made a different judgment in Section 4C as to how the balance should be struck among the distinct policies of encouraging enforcement, compensating the victims of antitrust violations, and judicial efficiency from this Court's subsequent judgment as to Section 4 in *Illinois Brick* does not make the Court or Congress right or wrong. Congress discharged its legislative function in creating a new remedy under Section 4C. See *Reiter v. Sonotone Corp.*, 442 U.S. at 344. The Court exercised its judicial function in interpreting Section 4. As the Court noted, Congress was free to change the balance with respect to indirect purchaser suits barred by *Illinois Brick*. 431 U.S. at 746. In fact, for claims brought by State Attorneys General as *parens patriae* on behalf of indirect consumer purchasers, Congress had already done just that in Section 4C.

CONCLUSION

For these reasons, the judgment below should be reversed.

Respectfully submitted,

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(10)

No. 88-2109

IN THE

Supreme Court of the United States

OCTOBER TERM, 1989

THE STATES OF KANSAS AND MISSOURI,
AS PARENS PATRIAE,
Petitioners,
v.

THE KANSAS POWER & LIGHT COMPANY

and

UTILICORP UNITED, INC.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF FOR THE STATE OF ILLINOIS AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF THE STATE OF ILLINOIS

Illinois has two distinct interests in this action. The first interest is the State's ability to vindicate consumer rights as *parens patriae* through an antitrust action. Title III of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (hereinafter "Hart-Scott-Rodino Act") empowers the States to bring antitrust actions on behalf of consumers. As one of the States that has taken the lead in enforcing the antitrust laws on behalf of its citizens,[1] Illinois has a strong interest in preserv-

[1] See, e.g., *Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S. Ct. 543 (1988) *on remand*, 58 U.S.L.W. 2429 (C.D. Ill. Jan. 2, 1990).

ing its right to represent and obtain recovery for its consumer citizens, be they direct or indirect purchasers.

Additionally, Illinois has a more immediate interest in the resolution of the legal issue presented in this case. In *Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Co.*, 852 F.2d 891 (7th Cir.) (en banc), *cert. denied*, 109 S.Ct. 543 (1988) (hereinafter "*Panhandle*"), the Seventh Circuit permitted Illinois to maintain an antitrust action on behalf of residential natural gas consumers overcharged by an interstate supplier of natural gas. The natural gas system in Illinois operates in essentially the same manner as the systems in place in Kansas and Missouri, and Illinois consumers were paying overcharges similar to those paid by Kansas and Missouri consumers. It is likely that the outcome of this case will be dispositive of the identical issue in *Panhandle* notwithstanding that the facts in *Panhandle* are somewhat stronger than the facts in the instant case.[2]

This Court should reverse the Tenth Circuit and approve the decision of the Seventh Circuit in *Panhandle* because, as contended by the States of Kansas and Missouri, the cost-plus exception to *Hanover Shoe* and *Illinois Brick* clearly applies to purchases of natural gas by residential consumers. Considering that—as we shall show—*Hanover Shoe* and *Illinois Brick* do not preclude this action from being maintained by an indirect purchaser consumer under § 4 of the Clayton Act, the Court need not address whether in some circumstances the

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appeal docketed, No. 90-1231 (7th Cir. 1990); *Illinois ex rel. Hartigan* v. *Matsushita Electric Corp. of America*, No. 89 Civ. 2789 (S.D.N.Y.) (settled 1989); *Greater Rockford Energy and Technology Corp. et al. and Illinois ex rel. Hartigan* v. *Shell Oil Co. et al.*, No. 88-2211 (C.D. Ill., Danville Division, filed June 1988); *Illinois ex rel. Hartigan* v. *Minolta Corp.*, No. 86-3075 (D. Md.) (settled 1987).

[2] After the Seventh Circuit sustained the Attorney General's right to file suit on behalf of consumers, the district court dismissed the case on the merits. See 58 U.S.L.W. 2429 (C.D. Ill. Jan. 2, 1990). The case is on appeal. 7th Cir. No. 90-1231.

Hart-Scott-Rodino Act authorizes a State to file a *parens patriae* action on behalf of an indirect purchaser even if such an action could not be brought by the indirect purchaser under § 4 of the Clayton Act.

This brief *amicus* describes in detail the regulatory system in Illinois and most other States which provides the factual context for this case as it did in *Panhandle*. The brief then applies the rationale of the *Hanover Shoe/ Illinois Brick* doctrine to that regulatory scheme. In the course of this discussion, we describe fully Judge Posner's analysis in *Panhandle* which is contrary to—and we submit much sounder than—the opinion of the court below in the present case. In this way, we seek to fulfill the obligation of an *amicus* to "bring[] relevant matter to the attention of the Court that has not already been brought to its attention by the parties." Cf. U.S. Supreme Court Rule 37.1.

SUMMARY OF ARGUMENT

In Point I of this Brief we show that in most States utility regulations require, as a matter of law, that the cost of natural gas to a utility be completely passed on to its residental customers (hereinafter "customers" or "consumers"). Because a utility receives revenue based upon its capital investment, it is entitled to recover its expenses from consumers. The utility's cost for gas from the pipeline company is not surprisingly treated as an operating expense of the utility. Furthermore, more than 40 States include "purchased gas adjustment" clauses (hereinafter "PGA clause") in the tariffs of utilities to ensure that all wholesale gas costs are passed on penny for penny regardless of fluctuations in the price of gas throughout the year.

PGA clauses function precisely like pre-existing cost-plus contracts. As our description of the operation of PGA clauses in Illinois demonstrates, the PGA clause itself is straightforward evidence that gas costs are

automatically passed-on. There can be no question that consumers are injured in the exact amount of that injury. No econometric models formulated to determine the effect on consumers of any overcharge by a pipeline need be introduced. Moreover, monthly and annual filings which utilities in Illinois are required to submit to the Illinois Commerce Commission specify the difference between the utility's actual costs as recorded in its books and the utility's revenue arising through its application of the Gas Charge formula. Additionally, consumers' monthly gas bills clearly identify the volume of gas delivered to and rate charged individual consumers. Hence, for each residential consumer of natural gas it can be established that (i) all natural gas costs were passed on to him or her and (ii) the exact volume and price of the purchased gas. Accordingly, it is easy to determine the damages incurred by individual consumers stemming from overcharges in the price of natural gas.

Point II of the brief demonstrates that the reasons for the general rule established in *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968) (hereinafter "*Hanover Shoe*"), and *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977) (hereinafter "*Illinois Brick*"), that only the direct purchaser may sue under § 4 of the Clayton Act for an illegal overcharge, are not present under the regulatory system described in Point I. "The *principal* basis for the decision in *Hanover Shoe*," wrote Justice White in *Illinois Brick*, "was the Court's perception of the uncertainties and difficulties in analyzing price and output decisions 'in the real economic world rather than an economist's hypothetical model,' 392 U.S. at 493, and of the costs to the judicial system and the efficient enforcement of the antitrust laws of attempting to reconstruct those decisions in the courtroom." 431 U.S. at 731-32 (emphasis added). Because the cost of any illegal overcharge must be passed on penny for penny by the utility to the consumer, and its amount is readily ascertainable under filings which the utility is required to make, the difficulties with which the Court was concerned in *Hanover Shoe* are eliminated. *Hanover Shoe* "recognize[d] that there might be situations—for instance, when an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged—where the considerations requiring that the passing-on defense not be permitted in this case would not be present." 392 U.S. at 494. Under the regulatory system here present, the conditions for such an exception are clearly satisfied.

Contrary to the view of the court below, *Hanover Shoe* did not decide and its rationale does not require that a pre-determined, "fixed quantity" of goods be contracted for in order to qualify for the "cost-plus" exception. No such limitation was stated in *Hanover Shoe*. As Judge Posner thoroughly explains in *Panhandle*, permitting consumers to maintain an action will not create an "apportionment" problem, as the Tenth Circuit believed in insisting upon a "fixed quantity" contract. This Court's concern in *Illinois Brick* was that apportioning the degree or extent of injury caused by the *same sale* would be extremely difficult, as well as burdensome, upon the judiciary. Under the facts of this case, however, the direct and indirect purchasers do not sue to recover for injuries caused by the same sale. Rather, consumers are suing for overcharges with respect to the gas they purchased, and utilities sue for damages due to lost sales. Determining the amount recoverable for such injuries is a familiar element of damage calculation in antitrust actions.

Because the nautral gas regulatory systems in Kansas and Missouri operate in essentially the same manner as Illinois' system, the foregoing analysis requires reversal of the judgment below.

ARGUMENT

I. AS A MATTER OF LAW IN ILLINOIS AND MOST OTHER STATES, THE COST OF NATURAL GAS IS PASSED ON, PENNY FOR PENNY, BY UTILITIES TO RESIDENTIAL CONSUMERS

A. Purchased Gas Adjustment Clauses Ensure That a Utility Passes on to Residential Consumers Its Entire Cost of Natural Gas, Notwithstanding Day to Day Fluctuations in the Price of Gas

Regulations in most States expressly provide that public utilities pass on their entire wholesale cost of natural gas to their customers, residential consumers, on a penny for penny basis. Underlying this practice is a fundamental element of public utility regulation: a public utility does not earn a profit on the gas it distributes. Rather, the utility receives a "revenue requirement" which provides the utility sufficient funds to cover its capital investment,[3] a reasonable rate of return on that investment and its operating expenses.[4] Foremost among these operating expenses is the wholesale cost of natural gas that the utility pays to its suppliers.[5] A $5 increase in the price of gas paid by the utility increases its operating expenses by $5, which increases its revenue requirement

[3] The primary component of the capital investment is the original cost of the utility plant in service, less depreciation. Other components included in the rate base by many States are materials and supplies, gas in storage and prepaid gas, and working capital. 2 American Gas Association, *Regulation of the Gas Industry* § 40.04[2][b] at 40-22 (1989).

[4] This can be translated into a simple formula: (Rate Base × Rate of Return) + Operating Expenses = Revenue Requirement. That revenue requirement is, of course, attained by charging customers for the gas that is delivered to them. As this formula indicates, there is a direct, one to one ratio between operating expenses and the revenue requirement. Thus, subject to regulatory review, operating expenses are included in the rates charged to consumers.

[5] 2 American Gas Association, *supra* note 3, § 26.03, at 26-6.

by $5. Thus, the utility can and must charge its customers precisely $5 more for that amount of natural gas it receives. When the cost of gas to a utility changes, the utility must change its rates in order that its revenue will reflect its changed operating expense.

The most commonly used mechanism for adjusting a utility's rates in response to changes in the wholesale price of gas is the "purchased gas adjustment" clause (hereinafter "PGA clause"). The origin and function of PGA clauses are described by Judge Posner in *Panhandle*:

> With the rapid and unanticipated increases in fuel prices during the 1970's, utilities pressed for and obtained the right to include automatic fuel pass-through provisions in their contracts with customers, provisions that would allow the utility to pass on every dollar in higher prices that it paid for gas or other fuels to its customers without going through the time-consuming process of obtaining regulatory authorization to raise rates. [A57.] [6]

In other words, PGA clauses establish a pre-existing mechanism by which increased wholesale gas costs to a utility will be *completely* passed on to its consumers.

B. Purchased Gas Adjustment Clauses Allow Residential Consumers to Prove Simply and Without Econometric Models That a Utility Has Passed its Natural Gas Costs on to Consumers (Indirect Purchasers) on a Penny for Penny Basis

PGA clauses are used in more than 40 States.[7] Though obviously different in certain details, they operate in es-

[6] Citations to *Panhandle* and the decision below will refer to the applicable page in the Appendix of the Petition for a Writ of Certiorari, in which the two decisions are reprinted at A43 *et seq.* and A1 *et seq.* respectively.

[7] National Assoc. of Regulatory Utility Commissioners, 1988 Annual Report 434-35. In States where PGA clauses are not used, retail gas prices may be adjusted if (i) a utility applies for a rate increase when the price of natural gas increases or (ii) the

sentially the same manner.[8] A review of the uniform PGA clause utilized in Illinois demonstrates how simple it is to prove that a utility's entire wholesale cost of natural gas has been passed on to its residential customers. The uniform PGA clause used in Illinois is prescribed in Illinois Administrative Code title 83, § 525 *et seq.*, and is set forth in the Appendix to this Brief. Illinois' PGA clause provides a utility with two options regarding how it may formulate its rate (called a "Gas Charge" in the PGA clause). Ill. Admin. Code tit. 83, § 525.10 (1985). The utility may charge a monthly rate based on a formula contained in § 525.20, or it may use a "base charge" and make monthly adjustments to conform to actual gas costs, as determined by that same formula.[9] In either event, the critical factor is that under the formula set forth at § 525.20, the full wholesale cost of gas is included as part of the "Gas Charge." Consequently, the entire cost of each utility's gas is passed on to consumers, regardless

State regulatory commission institutes a rate investigation. 2 American Gas Association, *supra* note 3, § 40.03, at 40-12 to 40-18.

[8] A number of States, including Illinois, have prescribed in their regulations the PGA clause to be used by all utilities within the State. These are called "uniform PGA clauses." In other States, the gas distributor submits its own clause for regulatory commission approval. 2 American Gas Association, *supra* note 3, § 40.06, at 40-88.

[9] The formula is:

$$GC = \frac{G + MG + SG \pm ST + PS \pm SE - C \pm RB}{P(1\text{-}U)} \times 100$$

This formula basically states that the Gas Charge (GC) equals the wholesale cost of natural gas (G) plus several other costs, divided by quantity (P represents the total units of gas delivered to the utility's customers from which is subtracted a small percentage representing gas which is unaccounted for (U)). The formula provides the utility with no leeway to absorb some of the increased costs of natural gas (or, conversely, to keep the gas charge at a steady rate when the cost of gas decreases).

of fluctuations in the price of gas to the utility.[10] Utilities are not permitted to charge any other price. Ill. Rev. Stat. ch. 111 2/3 ¶ 9-240 (1988).

The actual computation of the monthly Gas Charge under the PGA is strictly a mechanical function. The method by which CILCO computes its Gas Charge is illustrative. CILCO board members and senior management are not consulted. Ill. Br. App. at 37, para. 7. The actual responsibility to compute the Gas Charge is reposed with a lower level employee subject to supervisory oversight by CILCO's Manager of Rates & Regulatory Affairs and the Gas Supply Managers. Ill. Br. App. at 36, paras. 2-7. This clerk type employee has no discretion or authority to decline to pass on to CILCO's customers the cost of gas paid to Panhandle. Ill. Br. App. at 37. No economists need be consulted; and no econometric or other models need be applied. No costs are absorbed; the PGA clause must be and is followed.

A utility must file a monthly statement with the Illinois Commerce Commission specifying the Gas Charge that will be in effect for each succeeding month. Ill. Admin. Code tit. 83, § 525.10(d). Due to accounting differences between a utility and its suppliers, the gas rate charged consumers often does not fully correspond to the gas costs paid by the utility.[11] Under §§ 525.50 and

[10] For example, in 1983 and 1984, purchases of gas from Panhandle Eastern Pipeline Corp. by the Central Illinois Light Company (hereinafter "CILCO"), the direct purchaser of natural gas in *Panhandle*, amounted respectively to $181,472,132.18 and $165,664,969.60. Appendix to Brief for Appellee State of Illinois at 44 (7th Cir. No. 85-2601) (hereinafter "Ill. Br. App."). Every penny of the cost of this gas sold to CILCO flowed directly through to CILCO's customers pursuant to the uniform PGA clause.

[11] For example, according to Harold E. Shutt, Chief Engineer of the Illinois Commerce Commission in 1985, there is a time lag between when a wholesale cost increase occurs and when CILCO passes it on. This occurs for three reasons:

> (a) a lag occurs between the date Panhandle [the pipeline] delivers gas to CILCO and invoices CILCO; (b) a lag occurs

525.60, a utility submits an annual and a monthly filing which specifies the difference between the utility's actual costs as recorded in its books and the utility's revenue arising through its application of the Gas Charge formula. That balance (known as the "reconciliation balance") is refunded to the consumer when the utility has charged too much and is recovered by the utility when it charged too little, pursuant to a formula set forth in § 525.60. This ensures that the actual cost of natural gas is passed on penny for penny to the consumer.

C. The Information Contained in a Utility's Required Regulatory Filings and Its Monthly Gas Bills to Consumers Allow Residential Consumers to Establish Antitrust Damages Simply and Without Econometric Models

The monthly and annual filings a utility is required to submit pursuant to its PGA clause provide a readily accessible reference to the pricing and volume information needed by litigants to establish the price charged by a utility to its consumers, and the volume of gas sold. Furthermore, the Illinois Public Utilities Act requires that utilities make and maintain accurate accounting records. Ill. Rev. Stat. ch. 111 2/3 ¶¶ 5-102, 5-107 (1988).

Proving the injury incurred by an individual consumer is also extremely easy and straightforward. For example, Illinois requires that each monthly bill sent by CILCO to its customers contain the following three components:

> (1) an amount per customer not dependent on the amount of gas used; (2) an amount per therm of gas used, calculated to recover a share of fixed expenses and provide a profit margin; and (3) a gas charge factor. [*Panhandle* panel opinion, 839 F.2d

between the date CILCO delivers the gas to a customer and invoices the customer; and (c) a lag occurs between the date CILCO files its monthly PGA filing and the effective date of the filing. [Ill. Br. App. at 53.]

> 1206 at 1208 (7th Cir.), *rev'd*, on other grounds, 852 F.2d 891 (1988).]

See also Ill. Br. App. at 115; Ill Admin. Code tit. 83 § 500.330(a)(B); and Ill. Br. App. at 75-84, 85-103. Computing damages, therefore, requires no more than (i) calculating the difference between CILCO's purchase price of Panhandle's gas and the lawful price that would have been charged for the gas if no violation had occurred; (ii) dividing the total illegal overcharge by the number of units of Panhandle gas sold to compute the per unit amount of the overcharge; and (iii) multiplying the per unit amount of the overcharge by the number of units purchased by each consumer. Once the amount of the overcharge has been determined, calculating each consumer's damages is simple.

II. WHEN A PUBLIC UTILITY PASSES ON AN ILLEGAL OVERCHARGE, PENNY FOR PENNY, ITS CUSTOMERS AND THE STATE (AS *PARENS PATRIAE*) ARE THE PROPER PARTIES TO MAINTAIN AN ACTION UNDER *HANOVER SHOE* AND *ILLINOIS BRICK*

A. The Difficulties Which Led to the Result in *Hanover Shoe* and *Illinois Brick* Are Not Applicable Under the Regulatory System Described in Point I

As *Illinois Brick* made clear:

> In *Hanover Shoe*, this Court held that except in certain limited circumstances, a direct purchaser suing for treble damages under § 4 of the Clayton Act is injured within the meaning of § 4 by the full amount of the overcharge paid by it and that the antitrust defendant is not permitted to introduce evidence that indirect purchasers were in fact injured by the illegal overcharge. [431 U.S. at 724-25 (footnote omitted).[12]

[12] In the accompanying footnote, the Court said:

The Court [in *Hanover Shoe*] cited, as an example of when a pass-on defense might be permitted, the situation where "an

In *Illinois Brick*, the Court held, as a corollary, that an indirect purchaser should not be allowed to sue under § 4 on a pass-on theory to recover damages from a defendant unless the defendant would be allowed to use a pass-on defense in a suit by a direct purchaser.

The first ground articulated by the Court for applying the pass-on rule equally to plaintiffs and defendants was that "allowing offensive but not defensive use of pass-on would create a serious risk of multiple liability for defendants." *Id.* at 730. For, the Court explained:

> A one-sided application of *Hanover Shoe* substantially increases the possibility of inconsistent adjudications—and therefore of unwarranted multiple liability for the defendant—by *presuming* that one plaintiff (the direct purchaser) is entitled to full recovery while preventing the defendant from using that presumption against the other plaintiff; overlapping recoveries are certain to result from the two lawsuits unless the indirect purchaser is unable to establish any pass-on whatsoever. [431 U.S. at 730-31 (emphasis in original).]

This ground for decision is not germane to the present case because the dispute is between the utilities and the States as to *which* may sue the pipeline company. Both sides acknowledge that only one *or* the other may do so with respect to the injury resulting from the overcharges which were passed on to the residential consumers (indirect purchasers) of the natural gas.[13]

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overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged * * *" 392 U.S., at 494 * * *." [431 U.S. at 724 n.2.]

[13] It is not controverted that the direct purchaser utility company would retain the right to sue for lost profits, an injury and cause of action separate and distinct from the injury incurred by the consumer purchasers of the gas. See pp. 20-21 *infra*.

The second ground for rejecting use of offensive pass-on stated in *Illinois Brick* was that "the reasoning of *Hanover Shoe* cannot justify unequal treatment of plaintiffs and defendants with respect to the permissibility of pass-on arguments." 431 U.S. at 731. "The *principal* basis for the decision in *Hanover Shoe*," wrote Justice White in *Illinois Brick*, "was the Court's perception of the uncertainties and difficulties in analyzing price and output decisions 'in the real economic world rather than an economist's hypothetical model,' 392 U.S., at 493, and of the costs to the judicial system and the efficient enforcement of the antitrust laws of attempting to reconstruct those decisions in the courtroom." 431 U.S. at 731-32 (emphasis added). In an accompanying footnote, the Court demonstrated that

> this rationale was more important in the decision to bar the pass-on defense than the second reason [in *Hanover Shoe*]—the concern that if pass-on defenses were permitted indirect purchasers would lack the incentive to sue and antitrust violators would retain their ill-gotten gains, * * * is shown by the fact that the Court recognized an exception for pre-existing cost-plus contracts, which "mak[e] it *easy to prove* that [the direct purchaser] has not been damaged." 392 U.S. at 494. [431 U.S. at 732, n.12 (emphasis added in *Illinois Brick*).] [14]

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[14] The foregoing is confirmed by *Blue Shield of Virginia* v. *McCready*, 457 U.S. 465, 475 n.11 (1982):

> If there is a subordinate theme to our opinions in *Hawaii* and *Illinois Brick*, it is that the feasibility and consequences of implementing particular damages theories may, in certain limited circumstances, be considered in determining who is entitled to prosecute an action brought under § 4. Where consistent with the broader remedial purposes of the antitrust laws, we have sought to avoid burdening § 4 actions with damages issues giving rise to the need for "massive evidence and complicated theories," where the consequences would be to discourage vigorous enforcement of the antitrust laws by private suits. *Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*,

But the "uncertainties and difficulties," and consequent "costs to the judicial system * * *" which troubled the Court in *Hanover Shoe*, are eliminated by the regulatory scheme described in Point I of this Argument.

The Tenth Circuit made much of the question as to whether consumers or utilities would have a greater incentive to file suit. However, as the Court explained in *Illinois Brick*, this consideration was not decisive in *Hanover Shoe*:

> The amount of the stake that the customers of the direct purchaser have in a lawsuit against the overcharger is not likely to depend on whether they buy under a cost-plus contract or in a competitive market, but the Court allowed a pass-on defense in the former situation because the pre-existing cost-plus contract makes easy the normally complicated task of demonstrating that the overcharge has not been absorbed by the direct purchaser. [431 U.S. at 732, n.12.]

Just as the lack of incentive was not a reason for rejecting the cost-plus exception, it is not a reason to reject the exception in the present regulatory context.

B. *Hanover Shoe* Authorizes Indirect Purchasers Under Circumstances Akin to a Cost-Plus Contract to Maintain an Action Under Section 4 of the Clayton Act

Hanover Shoe did not establish a bar to the pass-on defense in any and all circumstances:

> We recognize that there might be situations—for instance, when an overcharged buyer has a preexisting "cost-plus" contract, thus making it easy to prove that he has not been damaged—where the

supra, at 498. Thus we recognized that the task of disentangling overlapping damages claims is not lightly to be imposed upon potential antitrust litigants, or upon the judicial system. See *Hawaii* v. *Standard Oil Co.*, 405 U.S. 251, 264 (1972); *Illinois Brick Co.* v. *Illinois*, *supra*, at 741-42.

> considerations requiring that the passing-on defense not be permitted in this case would not be present. [392 U.S. at 494.]

In *California v. ARC America Corp.*, 109 S.Ct. 1661, 1666 n.6 (1989), the Court stated with respect to its *Illinois Brick* decision that "[i]ndirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them." Because in this case the utility is required to pass on every penny of the overcharge, the cost thereof to the consumer is especially "easy" to prove, and "the considerations requiring that the passing-on defense not be permitted in [*Hanover Shoe*] would not be present." 392 U.S. at 494.

C. The Tenth Circuit Erred in Concluding that the Cost Plus Exception Must Include a Fixed Quantity Contract

The Tenth Circuit in the instant case "interpret[ed]" the cost-plus "exception as requiring a preexisting cost-plus contract for a fixed quantity." A8, *quoting Illinois Brick*, 431 U.S. at 735-36.[15] This view was squarely rejected by the majority of the *en banc* court in *Panhandle*. A45-A47.[16] It perhaps suffices that no such limitation was expressed in *Hanover Shoe*'s original for-

[15] The Tenth Circuit's quotation was as follows:

> *Hanover Shoe* indicated the narrow scope it intended for any exception * * * by citing, as the only example * * * a pre-existing cost-plus contract. In such a situation, the purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price. [*Id.*]

[16] It may be pertinent to note that *Panhandle* is not an instance of a decision in which a lower court, due perhaps to deeply-felt views, reads a precedent of this Court with a hostile eye. To the contrary, the opinion expresses strong approval of *Illinois Brick*: "An additional complication that further demonstrates the wisdom of the [*Illinois Brick*] *decision* * * *." [A49.]

mulation of the cost-plus exception (392 U.S. at 494, quoted at pp. 14-15, *supra*), and the circumstances of *Illinois Brick* provided no occasion for defining the contours of the exception. More fundamentally, as Judge Posner wrote in *Panhandle*:

> We do a disservice to the Court by wrenching its words out of context and giving them a talismanic significance; we make language a trap rather than a mode of communication. The Supreme Court has never adverted to the issue involved in the present case, and we must consider that issue in relation to the rationale of *Illinois Brick* rather than to isolated phrases in the Court's opinion. [A47.]

This is clearly the correct method for reading this Court's precedents. For, as Chief Justice Burger cautioned in sustaining the rights of consumers to sue under Clayton § 4, "the language of an opinion is not always to be parsed as though we were dealing with language of a statute." *Reiter* v. *Sonotone Corp.*, 442 U.S. 330, 341 (1979).

In sum, no "fixed quantity" limitation on the cost-plus exception has been established as a matter of *stare decisis*, as the Tenth Circuit thought. It remains to be determined whether such limitation *should be* adopted as a matter of principle, that is, in accordance with the rationale underlying *Hanover Shoe* and *Illinois Brick*. In support of that restriction, the Tenth Circuit said:

> The apparent reason for the fixed-quantity requirement to the cost-plus exception is simply that there would exist no problem of apportionment between the direct and indirect purchasers. In this case the problem of apportionment would exist even if all of the overcharge was passed on because there still exists the issue of decreased residential demand caused by the higher price. [A13.]

This cursory statement is based on a misconception of the "apportionment" problem which troubled this Court

in *Hanover Shoe* and *Illinois Brick*. In its thorough examination of this question in *Panhandle* (A50-A56), the Seventh Circuit carefully differentiated the problem of apportioning the cost of an overcharge along a chain of distribution which was involved in those cases from the problem of decreased residential demand as in *Panhandle* and in this case. Judge Posner did so in the context of demonstrating that "the reasons for confining the right to sue to the direct purchaser" (A49) do not require that the cost-plus exception be limited to "fixed quantity" contracts.

The *Panhandle* court began this part of its analysis by observing that "[w]here the direct purchaser has a cost-plus contract with his customers that requires them to buy a fixed quantity, * * * [t]here is no longer a problem of apportionment, because the whole of any price increase will have been passed on to the customers by virtue of the contract." A50.[17] In a case like *Panhandle* (and the instant case), the court continued, "where cost-plus pricing is imposed by public utility regulation rather than by a purely private, purely voluntary contract, the reasons balance out slightly differently, but the case for applying the cost-plus exception of *Illinois Brick* is no weaker once the balance is restruck." *Id.* For, "[a]lthough the amount of gas purchased by a utility's customers is not fixed in their contract with the utility * * *, the special character of a public utility eliminates the problem of apportionment, here with re-

[17] The second reason for confining the right to seek damages to the direct purchaser, the *Panhandle* court pointed out, "survives" under a cost-plus fixed-price contract. "Nevertheless the Supreme Court has said that the indirect purchaser may sue if he has a cost-plus contract with the direct purchaser." A50. This further confirms the primacy "of the uncertainties and difficulties" and "the costs to the judicial system and the efficient enforcement of the antitrust laws" to this Court's rejection of the pass-on theory in most circumstances. See *Illinois Brick*, 431 U.S. at 731-32, quoted at p. 13, *supra*.

spect to the only class of customers that we believe should be allowed to sue, the residential customers." A51.

We shall not here reiterate the court's entire demonstration of the foregoing proposition, but will confine ourselves to the points which bear most forcefully against the Tenth Circuit's view that a "fixed quantity" contract should be a prerequisite for applying a cost-plus exception to *Illinois Brick.* First, the *Panhandle* court showed why regulation performs the same function as does a fixed quantity commitment in situations where the free market is permitted to operate:

> The significance of the regulatory setting is that if regulation keeps a utility's rates below what it would like to charge, the utility will raise those rates by the full amount allowed by the regulatory commission unless such an increase would carry the utility above its optimum rate. An unregulated firm would not do that, since as we have noted an uncontested profit maximizer will always find it in its best interest to swallow a part of any cost increase that it experiences unless its customers are committed to a fixed quantity. [A53.]

The effect of the mandated pass-through provision was then explained:

> The "Uniform Purchase of Gas Adjustment Clause" that Illinois by statute requires CILCO to include in its contracts not only entitled but directed CILCO, if it paid Panhandle an extra penny per million cubic feet of gas, to add exactly one penny to each customer's bill for every Mcf of gas sold to that customer. So if all of its customers had continued buying the same amount of gas CILCO would have suffered no loss on account of the overcharge. [A53-54.]

The *Panhandle* court next turned to the loss due to the overcharge which the utilities do bear, and to which the Tenth Circuit in this case attached great significance:

> To the extent that CILCO lost residential sales because it was charging a higher price—and no doubt it lost some sales—the loss was not passed on to CILCO's customers (at least in any sufficiently direct way to escape the rule of *Illinois Brick*) and hence is not a component of the customer's damages. *But by the same token this is not a case where successive links in the chain of distribution are claiming damages in respect of the same transaction. There are, instead, two completely different sets of transactions.* One consists of sales to CILCO followed by resale to its residential customers; on these sales the entire overcharge came to rest on the residential customers and they alone suffered damage and can (on the view we take of the case) recover damages. The other set of transactions consists of the sales that CILCO lost because some customers balked at the higher rates; on these sales (or rather nonsales) the only loser is CILCO, and only CILCO can sue. [A54 (emphasis added).]

"Proof of loss of CILCO's lost sales," Judge Posner continued, "would also be straightforward—at least as straightforward as is possible in an antitrust case." A55. The task "is not always easy, but it is a conventional aspect of calculating damages in antitrust cases; it has to be done in every case where the plaintiff claims to have lost sales because of the defendant's unlawful conduct and the defendant argues that the loss was due partly or entirely to other factors." *Id.*, citing cases, including the familiar *Bigelow* v. *RKO Radio Pictures, Inc.*, 327 U.S. 251, 264 (1946). He then reached the heart of the matter:

> More important, it is a problem unrelated to the problem the Supreme Court wrestled with in *Hanover* and *Illinois Brick.* The Court was concerned with the situation where two purchasers of the same thing—the initial purchaser and the purchaser from the initial purchaser—are or could be complaining that both had been hurt, and the problem

> is to apportion the loss between them. Here only the residential consumers can complain about a loss from the overcharge on the gas they bought, while only CILCO can complain about a loss caused by the overcharge on gas that the residential consumers did not buy. [A56.]

The foregoing is entirely sound. *Hanover Shoe* illustrated the difficulty of showing "what effect a change in a company's price will have on its total sales" by listing the "wide range of factors [which] influence a company's pricing policies." 392 U.S. at 492-93. The essential point was that, due to the complexity of a company's pricing decisions, a determination of the impact of an illegal overcharge by each participant in the chain of distribution, as would be required to establish the applicability of the pass-on defense, would normally prove to be an "insurmountable" task. *Id.* at 493. The Court did not regard the difficulty of proving damages accruing from lost sales as an independent ground for disapproving the pass-on defense; as *Panhandle* pointed out, such calculation is a familiar aspect of antitrust damage suits. Nor did *Hanover Shoe* (or *Illinois Brick*) so much as suggest that when a particular antitrust violation causes different kinds of injury to different classes of plaintiffs, only one class may sue. Thus, contrary to the view of the Tenth Circuit (A11-12), any problem of apportioning damages in this case is entirely distinct from the problem in those cases.

Finally, because the injury to the consumer due to the overcharge and the injury to the utility from lost sales involve two completely different sets of transactions (A54), "the possibility of inconsistent adjudications—and therefore unwarranted multiple liability for the defendant" (431 U.S. at 730) is obviated here. Indeed, the Tenth Circuit did not seek to justify its conclusion even in part on the rationale that the defendant pipelines would be subject to duplicative recovery if the States, as

parens patriae, rather than utilities, are permitted to sue.[18]

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[18] *Blue Shield of Virginia* v. *McCready*, 457 U.S. 465 (1982) is especially instructive. There, a group health plan subscriber brought an antitrust action against her health insurer and an organization of Virginia psychiatrists alleging that the health plan's refusal to reimburse her for psychotherapy performed by psychologists was due to an unlawful conspiracy by defendants. This Court rejected the contention, among others, that *Illinois Brick* and *Hawaii* v. *Standard Oil Co.*, 405 U.S. 251 (1972), precluded her from suing under § 4 of the Clayton Act:

> *Both cases focused on the risk of duplicative recovery engendered by allowing every person along a chain of distribution to claim damages arising from a single transaction that violated the antitrust laws.* But permitting respondent to proceed in the circumstances of this case offers not the slightest possibility of a duplicative exaction from petitioners. McCready has paid her psychologist's bills; her injury consists of Blue Shield's failure to pay her. Her psychologist can link no claim of injury to himself arising from his treatment of McCready; he has been fully paid for his service and has not been injured by Blue Shield's refusal to reimburse her for the cost of his services. [457 U.S. at 474-475 (emphasis added).]

(The dissenting Justices did not base their conclusion on the theory that the subscriber may not sue under *Illinois Brick*. See *id.* at 486-92 (Rehnquist, J.), relying on the distinct standing limitation of *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 486-489 (1977). See also *id.* at 492-95 (Stevens, J.))

The only reference to *Hanover Shoe* or *Illinois Brick* in either dissenting opinion was the following:

> Those subscribers who did yield to Blue Shield's pressure suffer antitrust injury indirectly because of suppressed competition in the psychotherapy market. * * * I do not understand the Court to conclude that *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977), would not bar recovery by a subscriber, as opposed to a psychologist, in the latter situation. [457 U.S. at 487 n.2 (Rehnquist, J., dissenting).]

We believe that this is a correct reading of the majority opinion in *Blue Shield*, and that implicit therein is the dissenting Justices' understanding that the psychologists who lost patients due to the alleged violation could recover for that injury.

D. Under the Foregoing Analysis and the Facts of This Case the Judgment of the Tenth Circuit Must be Reversed

While the Illinois natural gas system discussed in *Panhandle* presented an especially strong case for allowing residential consumers (or the Attorney General for the State as *parens patriae*) to sue, the differences between *Panhandle* and this case do not call for a different result. The natural gas regulatory systems in Kansas and Missouri operate in essentially the same manner as Illinois' system.[19] Like Illinois, Kansas and Missouri both utilize PGA clauses to ensure that all natural gas costs are passed on from utility to consumer, both require that utilities file forms which place pricing and volume information in the public record, and consumers' gas bills in both States contain separate entries for the cost of gas.[20] Hence, proving that residential consumers are the true injured parties, and calculating the amount of their damages, is as easy in Kansas and Missouri as it is in Illinois. Even though the utilities have prosecuted their antitrust claims here, proving the separate and distinct injury suffered by residential consumers remains an equally simple endeavor, by virtue of the PGA clauses and the entire regulatory scheme.[21]

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[19] *See* Joint Brief of Plaintiff-Appellants the States of Kansas and Missouri in the court below, at 6-10, for a description of the operation of Kansas and Missouri's natural gas regulatory systems. This brief is referenced in the parties' Appendix in this Court and is therefore part of the record.

[20] *Id.* at 7-10.

[21] The Tenth Circuit relied on the fact that the present case involves "utilities occupying different levels on the distribution chain." A13. This refers to the fact that one of the three utilities that brought suit, Kansas Gas & Electric, does not distribute natural gas. A6. But this circumstance is entirely unrelated to the concern in *Hanover Shoe* and *Illinois Brick* that more than one person should not be permitted to recover on the basis of the same

CONCLUSION

For the foregoing reasons, the judgment of the Court of Appeals should be reversed.

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sale. In fact, Missouri and Kansas, on behalf of consumers, are not seeking recovery for overcharges paid by Kansas Gas & Electric (hereinafter "KG&E") because these overcharges were not passed on to the consumers. KG&E's participation in the suit against the pipeline does not make the suit more complex in any sense which affects the pass-on analysis. That KG&E does not distribute natural gas simply means that there is no need to determine who may bring suit regarding the overcharges paid by KG&E.

APPENDIX

APPENDIX

ILLINOIS ADMINISTRATIVE CODE

TITLE 83: PUBLIC UTILITIES
CHAPTER I: ILLINOIS COMMERCE COMMISSION
SUBCHAPTER d: GAS UTILITIES

PART 525
UNIFORM PURCHASED GAS ADJUSTMENT CLAUSE
(GENERAL ORDER 212)

Section

AUTHORITY: Implementing Section 36 and authorized by Section 8 of "AN ACT concerning public utilities" (Ill. Rev. Stat. 1981, ch. 111 ⅔, pars. 36 and 8).

SOURCE: Adopted at 6 Ill. Reg. 12437, effective September 30, 1982; emergency amendment at 7 Ill. Reg. 2002, effective February 1, 1983, for a maximum of 150 days; amended at 7 Ill. Reg. 7919, effective June 22, 1983; codified at 8 Ill. Reg. 12186.

Section 525.10 Rider: Gas Charge and Refund Adjustment Applicable to All Service Classifications

a) The Gas Charge and Refund Adjustments, applicable to all service classifications, shall be deter-

mined in accordance with the provisions of this rider.

AGENCY NOTE: The Gas Charge may be set forth in the utility's rate schedule in either of two forms:

1) a total charge determined monthly under the rider, in which case each individual service classification will contain a provision to the effect that the rates for service include a Gas Charge determined under the rider; or

2) a base charge stated in each individual service classification and there identified as the Gas Charge, subject to adjustments determined monthly under the rider.

This text of the rider assumes the first alternative. Where the second alternative is chosen, the utility must make appropriate revisions to the text.

b) Costs recoverable through the Gas Charge (Sections 525.20, 525.30 and 525.40), and annual reconciliation (Section 525.50 and Factor R4 of Section 525.60) shall include the cost of the following:

1) any solid, liquid or gaseous hydrocarbons purchased for injection into the gas stream, purchased as feedstock or fuel for the manufacture of gas, or delivered to the company under an exchange agreement,

2) storage service purchased under any rate, tariff or contract subject to regulation by a federal or state agency, and

3) transportation costs related to such solid, liquid or gaseous hydrocarbons and storage service.

c) The cost of the foregoing items shall exclude demurrage charges and penalty charges including but not limited to charges for late payment and unauthorized overruns and lost discounts. For exchange arrangements under which the company acquires gas for the purpose of supplying its distribution customers, costs recoverable through the Gas Charge and annual reconciliation shall include service charges, exclusive of interest and carrying charges, incurred by the company and recorded in Accounts 806 or 813. Determinations of the Gas Charge and annual reconciliation shall exclude the cost of gas used by the company, gas sold outside the company's distribution system, and gas delivered by the company under an exchange agreement. The cost of gas placed into storage inventory shall be included in the Gas Charge and annual reconciliation to the extent such gas is withdrawn from storage for sale to customers.

d) On or before the sixth day of each month, the company shall file with the Commission an information sheet specifying the Gas Charge and all Refund Adjustments to be effective for service rendered in the following month as provided in Section 525.20 and 525.60. Such filing shall include a statement showing the determination of such Gas Charge and the determination of a Refund Adjustment under Section 525.60, each determination to be accompanied by data in explanation thereof.

AGENCY NOTE: Where the determination of the Gas Charge includes the cost of a transaction between the utility and an unregulated affiliate, the computation sheet showing the transaction shall be footnoted to indicate that the transaction is with an affiliate.

e) As used in this rider:

1) the term "filing month" shall mean the month in which a Gas Charge or a Refund Adjustment is determined by the company and filed with the Commission;

2) the term "base period" shall mean the first 12 of the 13 months immediately preceding the filing month;

3) the term "applicable inventory price" shall mean the price applicable to gas capitalized or to gas or feedstock stored or withdrawn from inventory as reflected on the books of the company for a given month;

4) the term "system average cost of gas" shall mean, for a given month, the weighted average cost per therm of gas purchased and manufactured as reflected in Factors G and MG included in the Gas Charge filed in such month;

5) the term "gas used by the company" shall include all gas used by the company except gas utilized in the manufacture of gas through a reforming process reflected in Factor MG or Factor SG, and shall include gas furnished to municipalities or other governmental authorities without reimbursement in compliance with franchise, ordinance or similar requirements.

(Source: Amended at 7 Ill. Reg. 7919, effective June 22, 1983)

Section 525.20 Determination of Gas Charge

a) Each month the company shall determine under this Section the Gas Charge to be placed into effect with service rendered on and after the first day of the month following the filing month. Unless otherwise

ordered by the Commission, such Gas Charge shall become effective as indicated in the information sheet filed with the Commission and shall remain in effect until superseded under the terms of this rider.

b) The Gas Charge shall be determined in accordance with the following formula:

$$GC = \frac{G + MG + SG \pm St + PS \pm SE - C \pm RB}{P\,(1 - U)} \times 100$$

Where:

GC = The Gas Charge in cents per therm rounded to the nearest 0.01¢; any fraction of 0.01¢ shall be dropped if less than 0.005¢ or, if 0.005¢ or more, shall be rounded up to the next full 0.01¢.

G = The sum of the cost ($) of individual gas supplies as prescribed in Section 525.30.

MG = The sum of the cost ($) of individual manufactured gas supplies as prescribed in Section 525.30.

SG = The sum of the cost ($) of individual supplemental supplies as prescribed in Section 525.30.

St = The cost ($) of gas withdrawn from (+) and injected into (-) storage as prescribed in Section 525.30.

PS = The sum of the cost ($) of individual purchased storage services as prescribed in Section 525.30.

SE = The sum of the cost ($) of gas sold outside the company's distribution system (-) and gas delivered by the company (-) or delivered to the company (+) under an exchange agreement, as prescribed in Section 525.30.

C = The cost ($) of gas used by the company as prescribed in Section 525.30.

RB = An amount representing the estimated reconciliation balance ($) for the company's reconciliation year which includes the month following the filing month, as prescribed in Section 525.30 (costs in excess of revenues, +RB; revenues in excess of costs, -RB).

P = For the base period, the sum of therms of gas purchased, manufactured, withdrawn from storage and delivered to the company under an exchange agreement minus the sum of therms stored, used by the company, sold outside the company's distribution system, delivered by the company under an exchange agreement, utilized in the manufacture of gas through a reforming process reflected in Factor MG or Factor SG, and required as compressor fuel in connection with a storage service reflected in Factor PS.

U = Unaccounted for gas for the most recent 12 months ended (month) as a percentage of distribution sales plus unaccounted for gas for the same period, expressed as a decimal.

AGENCY NOTE: The utility shall use a 12 month period, ending with the month June, July or August, which had the lowest average percentage of unaccounted for gas determined by averaging the annual percentages for the preceding 5 years; once established the period must be consistently used until a change is approved by the Commission.

(Source: Amended at 7 Ill. Reg. 7919, effective June 22, 1983)

Section 525.30 Determination of Factors for Gas Charge Formula

The factors included in the Gas Charge formula under Section 525.20 shall be determined as follows:

a) Purchased Gas (Factor G)

For each gas supply purchased during the base period:

1) Multiply the number of units of demand (capacity) and units of commodity by the respective charges in effect on the first day of the filing month; if there is no purchase of a specific supply for the filing month, the last charge(s) paid for such supply purchased during the base period shall be used.

2) Add to the amounts determined under the foregoing paragraph (1) the cost for each such supply of any separately stated charge for transportation, based on the charge in effect on the first day of the filing month; if there is no purchase of such supply for the filing month, the last transportation charge paid for such supply purchased during the base period shall be used.

b) Manufactured Gas (Factor MG)

For each type of gas manufactured and made available to the company's distribution system during the base period:

1) Multiply the number of units of each supply feedstock or fuel purchased during the base period by the charge for such supply, including transportation, in effect on the first day of the filing month; if there is no purchase of a specific supply for the filing month, the last charge paid for such supply purchased during the base period shall be used.

2) For each supply of feedstock or fuel determine the difference between

A) the units of such supply placed into inventory during the base period multiplied

by the latest applicable inventory price for the base period, and

B) the units of such supply withdrawn from inventory during the base period multiplied by the applicable inventory price for the last month of the base period.

3) If in the foregoing determination (A) is larger than (B), the amount of such difference shall be assigned a negative value; if (B) is larger than (A), the amount of such difference shall be assigned a positive value.

c) Supplemental Gas (Factor SG)

For each supplemental gas supply (temporary and emergency) purchased or manufactured during the base period: multiply the number of units purchased each month of the base period by the rate charged for such month by the company's supplier and add transportation charges, if any; in the case of a supply initially accounted for as an inventory item, multiply the number of units taken from inventory each month of the base period by the applicable inventory price for such month.

d) Storage Gas (Factor St)

For each type of gas storage facility, determine the difference between

1) the units of gas capitalized or inventoried during the base period multiplied by the applicable inventory price for the last month of the base period or, in the case of gas returned to cushion, by the average cost of all gas previously withdrawn from cushion; and

2) the units of gas withdrawn from storage during the base period multiplied by the applicable inventory price for the last month of the base

period or, in the case of gas withdrawn from cushion, by the system average cost of gas for the month in which such withdrawal is made.

3) If the foregoing determination (1) is larger than (2), the amount of such difference shall be assigned a negative value; if (2) is larger than (1), the amount of such difference shall assigned a positive value.

e) Purchased Storage Service (Factor PS)

For each storage service purchased during the base period under a rate, tariff or contract subject to regulation by a federal or state agency:

1) Multiply the units of demand (capacity) and units of commodity by the respective charges in effect on the first day of the filing month; if there is no purchase of a specific storage service for the filing month, the last charges paid for such storage service purchased in the base period shall be used.

2) Add to the amounts determined under the foregoing paragraph (1) the cost for each such storage service of a separately stated charge for transportation based on the charge in effect on the first day of the filing month; if there is no purchase of a specific storage service for the filing month, the latest transportation charge paid for such storage service purchased during the base period shall be used.

f) Sales and Exchanges (Factor SE)

1) For gas sold outside the company's distribution system, multiply the sum of the units of gas sold during each month of the base period by a unit cost equal to the Gas Charge filed during each such month exclusive of the effects of Factor RB and Refund Adjustments under Section

525.60. The total of amounts determined under this paragraph shall be assigned a negative value.

2) For gas delivered by the company under an exchange agreement, multiply the units of gas delivered during each month of the base period by the system average cost of gas for each such month, or in the case of gas returned by the company under an exchange agreement, by the applicable unit cost of gas to be returned under such agreement as reflected on the books of the company for each such month. The total of amounts determined under this paragraph shall be assigned a negative value.

3) For gas delivered to the company under an exchange agreement, multiply the units of gas delivered during each month of the base period by the system average cost of gas for each such month, or in the case of gas returned to the company under an exchange agreement, by the applicable unit cost of gas to be returned under such agreement as reflected on the books of the company for each such month. Add to the amounts determined under the foregoing sentence any transportation charges and service charges, exclusive of interest and carrying charges, incurred by the company and recorded in Accounts 806 or 813 for each month of the base period for each exchange arrangement under which the company acquires gas for the purpose of supplying its distribution customers. The total of amounts determined under this paragraph shall be assigned a positive value.

g) Company Use (Factor C)

For gas used by the company during the base period: multiply the number of units used by the company by the system average cost of gas for the

filing month. For the purposes of this rider, gas used by the company shall include gas furnished to municipalities or other governmental authorities without reimbursement in compliance with franchise, ordinance or similar requirements; gas used by the company shall not include gas utilized in the manufacture of gas through a reforming process reflected in Factor MG or Factor SG.

h) Reconciliation Balance (Factor RB)

Each month the company shall determine, in the manner contemplated by Section 525.50, the anticipated reconciliation balance for the reconciliation year which includes the month following the filing month. If in such determination anticipated revenues exceed or fall short of anticipated costs by more than one-half of one percent, the anticipated reconciliation balance shall constitute the amount to be reflected as Factor RB in the determination of the Gas Charge to be effective for service rendered in the month following the filing month; the same amount shall be reflected as Factor RB in the determinations of Gas Charges to be effective for service rendered in the remaining months of the same reconciliation year unless a subsequent determination under this paragraph requires a change. If the anticipated reconciliation balance represents costs in excess of revenues, Factor RB shall be assigned a positive value; if the anticipated reconciliation balance represents revenues in excess of costs, Factor RB shall be assigned a negative value.

(Source: Amended at 7 Ill. Reg. 7919, effective June 22, 1983)

Section 525.40 Changes in Gas Supply

Where a change in gas supply occurs during the month prior to the filing month and would cause the revenues

arising through the application of the Gas Charge for the 12-month period beginning with the month following the filing month to exceed or fall short of the costs recoverable through the Gas Charge for the same period by one-half of one percent or more, the company shall reflect such change in the determination of the Gas Charge to become effective with service rendered in the month following the filing month by adjusting on an annual basis the units of supply for each factor affected by such change. Such change shall be reflected in subsequent determinations of the Gas Charge until it is fully reflected in the units of supply for the base period. The company shall, in the statement showing the determination of the Gas Charge, identify those factors which reflect such change. For the purposes of this paragraph, the revenues arising through the application of the Gas Charge and the costs recoverable through the Gas Charge shall be determined in the manner contemplated by Section 525.50, except that such revenues shall not include the effect of Factor RB.

Section 525.50 Annual Reconciliation

a) Within 60 days after the end of each reconciliation year, the company shall file with the Commission a statement showing the determination of the reconciliation balance for such year; certified by the company's independent public accountants and verified by an officer of the company. The reconciliation balance shall be the difference between

1) the costs recoverable through the Gas Charge as recorded on the books of the company for such year, exclusive of any credits or debits relating to amounts reflected in factors of the Refund Provisions of Section 525.60, and

2) the revenues arising through the application of the Gas Charge to therms sold by the company during such year, exclusive of the effect of Refund Adjustments under Section 525.60. In the determination of costs recoverable through the Gas Charge under the foregoing sentence, the cost assigned to gas sold outside the distribution system shall be reflected as a credit. The reconciliation balance shall be refunded or recovered under R4 of the Refund Provisions of Section 525.60. If the reconciliation balance represents costs in excess of revenues, Factor R4 shall be assigned a negative value; if the reconciliation balance represents revenues in excess of costs, Factor R4 shall be assigned a positive value. The company's reconciliation year shall be the 12-month period ending the — day of (month).

AGENCY NOTE: The cost assigned to gas sold outside the distribution system shall be determined for each sale by order of the Commission.

b) Unless otherwise ordered by the Commission, the company shall include the reconciliation balance in the Refund Adjustment calculated and filed with the Commission in the third month following such reconciliation year. If upon hearing under the fifth paragraph of Section 36 of the Illinois Public Utilities Act, the Commission finds that the reconciliation balance for such reconciliation year should be higher or lower than such balance as reflected in a Refund Adjustment previously made effective under Section 525.60, the difference between the reconciliation balance as found by the Commission and such balance as reflected in a Refund Adjustment shall be refunded or recovered, as appropriate, under R4 of the next Refund Adjustment made effective under Section 525.60.

(Source: Amended at 7 Ill. Reg. 7919, effective June 22, 1983)

Section 525.60 Refund Provisions

a) Each month the company shall determine a Refund Adjustment under this Section. If such Refund Adjustment computes to 0.01¢ per therm or more, it shall be subtracted from the Gas Charge over an annual billing cycle beginning with service rendered on and after the first day of the month following the filing month. If such Refund Adjustment does not compute to at least 0.01¢ per therm, the amounts reflected in the determination shall be retained in a Refund Due Customer Account until an adjustment subsequently determined under this Section, including any amounts so retained, computes to at least 0.01¢ per therm. The monthly determination of a Refund Adjustment shall be included in the statement filed with the Commission in connection with the Gas Charge.

b) Refund Adjustments shall be determined in accordance with the following formula:

$$RA = \frac{R1 - R2 + i(R1 - R2 \pm R4) \pm R3 \pm R4 + R5 + R6}{P(1 - U)} \times 100$$

Where:

RA = The Refund Adjustment in cents per therm; provided that if the adjustment computes to 0.01¢ per therm or more, any fraction of 0.01¢ shall be dropped if less than 0.005¢ or, if 0.005¢ or more, shall be rounded up to the next full 0.01¢.

R1 = Any amount including interest received by the company from a supplier during the second month prior to the filing month by reason of any refund, adjustment, rebate or credit of charges paid by the company and used in the calculation of the Gas Charge.

R2 = Increases in charges made effective retroactively to months prior to the filing month and applicable to such supplies previously purchased and charged to gas distribution system customers under Factors G, MG, SG and PS of the Gas Charge.

R3 = Amount due customers (+R3) or amount due the company (-R3) as a consequence of any prior Refund Adjustment, computed at the termination of the appropriate billing cycle ending during the second month prior to the filing month.

R4 = The annual reconciliation balance for the preceding reconciliation year determined under Section 525.50 (costs in excess of revenues, -R4; revenues in excess of costs, +R4).

R5 = A credit for sales made outside the company's distribution system during the second month prior to the filing month equal to one-half of the difference between the revenue billed for such sales and the cost assigned to the gas sold plus other direct expenses.

AGENCY NOTE: The cost assigned to the gas sold and other direct expenses shall be determined for each sale by order of the Commission.

R6 = The amount to be refunded by reason of the refund provision of (rider relating to incremental pricing) for the second month prior to the filing month.

i = An interest factor of 6⅔%, expressed as a decimal, to be applied to the total of R1, R2 and R4.

AGENCY NOTE: The factor of 6⅔% represents an annual rate of 10% of the unrefunded balance of R1, R2 and R4 over a 14-month period, assuming that the full balance is outstanding for two months, the approxi-

mate period before items reflected in Factors R1, R2 and R4 would begin flowing through a Refund Adjustment, and that the balance declines by one-twelfth of the total of R1, R2 and R4 each month over the annual billing cycle of 12 months during which a Refund Adjustment would be reflected in rates.

P = Same as for GC formula.

U = Same as for GC formula.

c) Should a Refund Adjustment more nearly pay out at the end of 11 or 13 months, the refund period may be shortened or lengthened accordingly upon the company giving 25 days' notice to the Commission of the change in the refund period.

(11)

No. 88-2109

In the Supreme Court of the United States

OCTOBER TERM, 1989

THE STATES OF KANSAS AND MISSOURI, AS *PARENS PATRIAE*,
Petitioners

v.

THE KANSAS POWER & LIGHT COMPANY and
UTILICORP UNITED, INC.,
Respondents

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF *AMICI CURIAE* AND BRIEF *AMICI CURIAE* OF NANCY ALLEVATO, Personal Representative of MICHAEL J. FERRANTINO, SR., DECEASED, *et al.* IN SUPPORT OF PETITIONERS

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March 1, 1990

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No. 88-2109

In the Supreme Court of the United States

OCTOBER TERM, 1989

THE STATES OF KANSAS AND MISSOURI, AS *PARENS PATRIAE*,
Petitioners

v.

THE KANSAS POWER & LIGHT COMPANY and
UTILICORP UNITED, INC.,
Respondents

**On Writ of Certiorari to the
United States Court of Appeals for the Tenth Circuit**

MOTION FOR LEAVE TO FILE BRIEF *AMICI CURIAE*

Nancy Allevato, personal representative of Michael J. Ferrantino, Sr., deceased, *et al.*, hereby respectfully move for leave to file the attached Brief *Amici Curiae* in Support of Petitioners in this case. The consents of the attorney for petitioner the State of Missouri and the attorneys for respondents have been obtained. Consent of the attorney for petitioner the State of Kansas was requested but not obtained.

As more specifically stated in the Brief *Amici Curiae*, the interest of *Allevato, et al.* arises from the fact that they are Petitioners in *Allevato* v. *County of Oakland*, No. 89-56 (U.S. filed July 13, 1989) (*petition for cert. pending*), the outcome of which is likely to be affected by the Court's disposition of this case. Specifically, the Court's disposition of this case will determine whether direct purchasers have standing under Section 4 of the Clayton Act, 15 U.S.C. §15(a), where it was clear from the outset of a transaction that the direct purchasers have passed on 100 percent of all overcharges allegedly resulting from antitrust violations.

The Solicitor General, in his Brief *Amicus Curiae* for the United States in *Allevato*, recommended that the *Allevato* petition for certiorari be held by the Court pending the outcome in the case at bar.

The persons and entities making this motion believe that their participation in litigation similar to this case provides them with a perspective on the questions presented that will be useful to the Court, and that is different from the perspective of the parties.

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BRIEF *AMICI CURIAE* of NANCY ALLEVATO, Personal Representative of MICHAEL J. FERRANTINO, SR., Deceased, *et al.* IN SUPPORT OF PETITIONERS

STATEMENT OF INTEREST OF *AMICI CURIAE*

Amici curiae are the Petitioners in *Allevato* v. *County of Oakland*, No. 89-56 (U.S. filed July 13, 1989) (*petition for cert. pending*), the outcome of which is likely to be affected by the Court's disposition of this case. *Amici curiae* file this Brief in support of the Petitioners in this case. In *Allevato*, the Michigan counties of Oakland and Macomb (the "Counties"), which purchased sewerage services and various components directly from *amici curiae* and others, sued, alleging a conspiracy to illegally overcharge for the services in violation of the federal antitrust laws and RICO. It is undisputed that the Counties, as required by Michigan statutes, passed on all of the price of sewerage services, including any alleged overcharges, to subsequent purchasers.

In *Allevato*, the plaintiffs/Respondents are direct purchasers who seek to sue for injuries that were passed on by them to indirect purchasers. In the case before the Court, the plaintiffs/Petitioners are indirect purchasers who seek to sue for injuries that were passed on to them by direct purchasers. In deciding whether indirect purchasers may bring suit in this case, the Court is likely to articulate the legal rules that govern *Allevato* as well.[1]

SUMMARY OF ARGUMENT

The very essence of a private cause of action for damages under the federal antitrust laws is to provide relief to any person "who shall be injured in his business or property by reason of anything forbidden in the antitrust laws * * *." 15 U.S.C. §15(a) (1982). Regardless of any policy considerations, a party must have been *injured* in order to maintain an antitrust action. Despite this obvious proposition, the court below held that only direct purchasers have standing to maintain antitrust actions even though the direct purchasers have, by virtue of contractual, regulatory or statutory requirements, suffered no injury because they passed on 100 percent of any allegedly unlawful overcharge to end-user customers — the so-called "perfect" pass on.

The question presented in the case at bar, *Kansas* v. *The Kansas Power & Light Co.*, No. 88-2109 (U.S. filed June 26, 1989), *cert. granted*, 58 U.S.L.W. 3449 (U.S. Jan. 16, 1990), is whether the direct or indirect purchaser has standing to sue defendants (not involved in the case before the Court) where "there is an easily proven, 100% pass-on of illegal overcharges * * *." (Pet. at I). In both this case and *Allevato*, one essential fact is clear — that the direct purchaser suffered no damages because it did not absorb any portion of the alleged unlawful overcharge.

Hanover Shoe, Inc. v. *United Shoe Machinery Corp.*, 392 U.S. 481 (1968), and *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977),

[1]The Solicitor General has recognized that the decision in this case could resolve the issues presented by *Allevato*. *See* Brief for the United States as *Amicus Curiae* in *Allevato* at 8-9. There are also some differences between this case and *Allevato*. *See* discussion, *infra*, at 10-11.

both involved making a *policy* choice; whether to confer standing on the direct purchaser, indirect purchaser, or both in a situation where there were multiple levels in the relevant economic distribution chain and it was determined that some injury was suffered at each level, although the amount of injury at each level was not readily ascertainable. Where damages could have been suffered at each level and where each level could have absorbed a portion of the overcharge, the Court had a policy choice to make as to whether to prefer the direct or indirect purchaser or whether to have trial courts engage in the costly and potentially impossible exercise of apportionment of the damages. In opting to prefer the direct purchaser, the Court took into account various policy considerations.

Such policy considerations, however, are pertinent *only* in situations where both parties were injured by absorbing overcharges. *Illinois Brick* and *Hanover Shoe* do not, however, stand for the proposition that uninjured parties are to be made "preferred surrogates" who can maintain private antitrust actions simply because they are the direct purchasers in an economic chain of distribution. The choice as between direct and indirect purchaser need not, and legally should not, be made where the direct purchaser was not injured.

Efforts by the Sixth and Tenth Circuits to make uninjured direct purchasers surrogate plaintiffs simply because they do not fit within the exact wording of the cost-plus "exception" not only turn the concept of standing on its head, but may result in those surrogates making enforcement decisions which are not consistent with the remedial purposes behind the antitrust laws. Uninjured surrogate plaintiffs are poor private attorneys general because they do not suffer actual monetary loss (the accepted bellwether of antitrust injury) and are not motivated by the need to make themselves whole. Thus, by giving an uninjured direct purchaser the exclusive right to maintain an antitrust action in these circumstances, the Court may actually defeat the remedial purposes behind the antitrust laws, as the uninjured surrogate, having suffered no damages at all, simply may choose not to sue. Because the antitrust laws are intended to compensate victims of antitrust violations for their injuries, *Illinois Brick*, 431 U.S. at 746 (citing

Brunswick Corp. v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 485-86 (1977)), only the injured persons should be entitled to bring suit.

Allevato and the case at bar are different in that *Allevato* does not involve a situation where a decrease in demand by the indirect purchasers could conceivably harm the direct purchasers by causing a loss in profits. Thus, should the Court rule that the possibility of a decrease in profits due to a decrease in demand because of an overcharge dictates that only the direct purchaser has standing, the Court should still summarily reverse or remand in *Allevato*.

ARGUMENT

I. THE RULE SET FORTH IN *HANOVER SHOE* AND *ILLINOIS BRICK* DOES NOT JUSTIFY ALLOWING UNINJURED DIRECT PURCHASERS IN THE CHAIN OF DISTRIBUTION TO HAVE STANDING.

A. Granting Standing Only to Uninjured Direct Purchasers Ignores the Essential Purposes of Section 4 of the Clayton Act.

The legislative history of Section 4 of the Clayton Act, 15 U.S.C. § 15(a) (1982) and the original treble damages provision, Section 7 of the Sherman Act, 26 Stat. 210 (1890), shows that the treble damages provision was an incentive linked to injury. *See Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 485-86 & n.10 (1977) (citing legislative history of Section 7 of the Sherman Act). Congress could have legislated a treble damages "bounty" as an incentive for anyone to sue for injury to the marketplace if maintaining the action and penalizing the violator were more important than compensating the victims of antitrust violations.[2] Because Congress linked the treble damages incentive to injury, *see, e.g. Hawaii* v. *Standard Oil Co.*, 405 U.S. 251, 262-63 (1972), the Court should not break the linkage by granting standing to the uninjured. This centennial year of the Sherman Act provides a particularly appropriate occasion for this Court to reaffirm and clarify that Section 4 is indeed a remedial provision and cannot in any way be construed to give standing to persons not injured by alleged antitrust violations, while overlooking those who were injured.

[2]Other statutes provide "bounties" to "deputized" uninjured persons who bring *qui tam* actions against malfactors. *See, e.g.*, False Claims Act, Section 232, 31 U.S.C. § 3730 (Supp. 1989); *United States ex rel. Marcus* v. *Hess*, 317 U.S. 537 (1943); *Public Interest Bounty Hunters* v. *Board of Governors of the Federal Reserve System*, 548 F. Supp. 157, 161 (N.D. Ga. 1982). Such statutes are not linked to injury and demonstrate that Congress could have granted uninjured parties antitrust standing, and the treble damages incentive, if it so desired.

When direct and indirect purchasers in the same chain of distribution are subjected to allegedly unlawful overcharges, four possible results could occur. First, the direct purchaser could absorb all the overcharges. Exclusive direct purchaser standing in this situation is beyond dispute. Second, both the direct and the indirect purchasers could absorb a portion of the overcharge, but the amount of each portion is either difficult or impossible to determine. This was the situation in *Hanover Shoe* and *Illinois Brick*, where the direct purchaser in a competitive resale marketplace, in order to maximize profits, absorbed part of the overcharge.[3] The forces determining the amount absorbed by the direct purchaser are the elasticities of supply and demand. The Court in *Hanover Shoe* and *Illinois Brick* determined that the direct purchaser should have standing where apportionment of the damages caused by the overcharges requires an analysis of the complex interaction of these forces. Third, as occurred in the case at bar and in *State of Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Corp.*, 852 F.2d 891 (7th Cir.) (*en banc*), *cert. denied*, ___ U.S. ___, 109 S.Ct. 543 (1988), the direct purchaser, because of regulatory or contractual reasons, either must pass on or finds that it is in its economic interest to pass on 100 percent of the alleged overcharge to its customers, yet still faces a possible decrease in profits when the higher price leads to a decrease in demand for its goods or services. The fourth case, such as in *Allevato*, is where

[3]In *State of Illinois ex rel. Hartigan* v. *Panhandle Eastern Pipe Line Corp.*, 852 F.2d 891, 894 (7th Cir.) (*en banc*), *cert. denied*, ___ U.S. ___ 109 S.Ct. 543 (1988), Judge Posner observed that "[t]he optimal adjustment by an unregulated firm to the increased cost of the input will *always* be a price increase smaller than the increase in input cost, and this means that the increased cost will be divided between the two tiers, the direct and indirect purchasers * * *." (emphasis added). In other words the direct purchaser, realizing its customers will purchase less if it charges them higher prices, will determine the minimum amount of the overcharge to absorb so that the loss caused by decreased demand, combined with the absorbed portion of overcharges, will be minimized.

the direct purchaser is fully insulated from any injury, whether the injury results from an overcharge or from lost profits due to decreased demand. The insulation from lost profits due to decreased demand can occur because the direct purchaser is not a profit-making entity or because it has a pre-existing cost-plus contract for a fixed quantity with indirect purchasers.

The only issue before the Court is whether direct purchasers who pass on 100 percent of an allegedly unlawful overcharge (which occurs in the third and fourth scenarios described above) have standing to sue for injuries allegedly resulting from the perfectly passed on unlawful overcharges *and* from any decrease in profits due to decreased demand from the pass on. No reading of *Hanover Shoe* or *Illinois Brick*, which address only overcharges absorbed by both direct and indirect purchasers (the second scenario described above), could justify conferring standing on the direct purchasers in the third or fourth situations. Actions by direct purchasers for injuries clearly and conclusively not sustained by them contravenes the remedial intent of Section 4, and leaves those who are truly injured without effective relief. In addition, the direct purchasers will obtain windfall treble recoveries, which were specifically intended to give the truly injured party the necessary incentive to sue.

The following three subsections discuss in detail the second, third and fourth possible situations, noted above, where a direct purchaser is subjected to an unlawful overcharge.

1. *Hanover Shoe* and *Illinois Brick* Apply Only Where Apportionment of Unlawful Overcharges Cannot Reasonably Be Calculated.

Hanover Shoe and *Illinois Brick* established a rule giving preference to direct purchasers only in the second situation described above, where the direct and indirect purchasers both absorbed part of any allegedly unlawful overcharge, and apportionment of damages between them is impossible or impracticable. The Court specifically stated that apportionment of the overcharges would necessitate resorting to a complex analysis of the interactions of the forces of supply and demand, including an analysis of the

relative elasticities of supply and demand. *See, e.g., Illinois Brick*, 431 U.S. at 732. Where both the direct and indirect purchasers clearly suffered some degree of injury from the alleged overcharge and where any attempt to apportion such damages "would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge — from direct purchasers to middlemen to ultimate consumers," 431 U.S. at 737, the direct purchasers should and would be elevated to the preferred position. The Court noted that "it is unrealistic to think that elasticity studies introduced by expert witnesses will solve the pass on-issue." *Id.* at 742.

The Court made a *policy* decision to prefer direct purchasers. This decision was based on two considerations. First and primary was that of maintaining the efficiency of treble-damages actions. Engaging in "vertical" apportionment, among parties at different levels of the chain of distribution would be either impossible or impractical. The second consideration was assuring vigorous enforcement of the antitrust laws. The Court reasoned that where apportionment of the injury would be costly and indirect purchasers would have a potentially small stake in the litigation, the direct purchaser would be in a better position to vindicate the marketplace through private enforcement of the antitrust laws. *Illinois Brick*, 431 U.S. at 744.[4]

The Court's analysis of these important public policy considerations undertaken in *Illinois Brick* and *Hanover Shoe* is unnecessary in the case at bar and in *Allevato* because neither case involves different parties along an economic chain of distribution who are claiming to have suffered *the same* injury from absorbing an overcharge, or a part thereof. In both cases it was apparent from the outset which party in the distribution chain absorbed the alleged unlawful overcharges.[5] Thus, the reason for elevating

[4] The Court found this consideration secondary to the former, "ease of apportionment" consideration. *See Illinois Brick*, 431 U.S. at 732 n.12; *California v. ARC America Corp.*, 490 U.S. ___ ___ n.6, 109 S.Ct. 1661, 1666 n.6 (1989).

[5] It cannot be argued that the simple determination of a perfect pass on implicates the complexities giving rise to the rule in *Hanover Shoe* and *Illinois Brick*. *See Panhandle*, 852 F.2d at 898 ("we *know* that the whole overcharge was passed on to the customers * * *").

the direct purchaser to a preferred position evaporates. *See Hanover Shoe*, 392 U.S. at 494; *Illinois Brick*, 431 U.S. at 732 n. 12.

2. As Petitioners Argue, Whenever a Perfect Pass On of 100 Percent of an Overcharge Occurs, Indirect Purchasers Should Have Standing to Sue for the Overcharge.

The forces necessitating the policy choice made in *Hanover Shoe* and *Illinois Brick* for exclusive direct purchaser standing for all injuries (including injuries from paying the overcharge and injuries caused by a decrease in sales) are not present in all situations, and are not present in the case at bar and in *Allevato*. To ignore these situations and grant the direct purchaser exclusive standing simply because a transaction lacks the "fixed-quantity" element would make the goals of the antitrust laws less likely to be met. *Panhandle* recognized this and held that even in the absence of a cost-plus contract for a "fixed quantity," the direct purchaser should not be a surrogate plaintiff where the effect of the overcharge can be determined in advance without reference to the interaction of supply and demand. Clinging to terms such as "fixed-quantity" as a talismanic substitute for analysis of the true economic structure of the transaction at issue leads to illogical and improper results. *See Panhandle*, 852 F.2d at 893.[6]

[6]Given the lack of guidance in applying the rule established in *Hanover Shoe* and *Illinois Brick*, lower courts have ignored the rationale behind the policy choice for direct purchaser standing and the "exceptions" thereto and have engaged in illogical, result-oriented reasoning to grant standing to direct purchasers. The Sixth Circuit in *County of Oakland* is a prime example. Although the Sixth Circuit acknowledged that "100% of the charges [and alleged overcharges] imposed by Detroit [on the Counties] were passed on by the [Counties] to the municipalities, which would make the [Counties] a 'conduit' in an economic sense," 866 F.2d at 845, the court, ignoring injury altogether, still found that the complexities of apportioning the damages *among* purchasers at the *same level* of distribution would "invite precisely the sort of complexities, uncertainties, and other untoward consequences that the indirect purchaser rule was designed to avoid." 866 F.2d at 849. To carry this rationale to its logical conclusion would emasculate federal class action suits in any situation where the apportionment of damages among the members of the injured class would be complex or uncertain. Even aside from the fact that the Counties absorbed no portion of the overcharge, the court's application of the "apportionment consideration" was incorrect. The complexities giving rise to the "direct purchaser rule" in *Hanover Shoe* and *Illinois Brick* stemmed from the nearly impossible task of analyzing the forces of supply and demand in apportioning damages among purchasers on *different levels* of an economic distribution chain. (*Allevato* Pet. at 16). Moreover, the Sixth Circuit, in its discussion of constitutional standing, found that the Counties were harmed because the alleged overcharges *may* have deterred businesses or individuals from remaining in and/or relocating to the Counties. These types of "injuries," if they be injuries at all, are simply not cognizable under the antitrust laws. (*Id.* at 11-12, 23; *Allevato* Reply at 5-6).

The example of the cost-plus exception in *Hanover Shoe* and *Illinois Brick* was the Court's recognition that situations exist where:

> The effect of the overcharge is essentially determined in advance, without reference to the interaction of supply and demand that complicates the determination in the general case.

431 U.S. at 736; *see also Hanover Shoe*, 392 U.S. at 494. There is no indication that the cost-plus "exception" was intended to be an exclusive exception to the direct purchaser rule. *See Panhandle*, 852 F.2d at 893. The non-exclusivity of exceptions to direct purchaser standing is further shown by the fact that the Court suggested another exception, the "control" exception (*e.g.*, the direct purchaser is owned or controlled by the indirect purchaser), *see Illinois Brick*, 431 U.S. at 736 n.16, where the policy considerations favoring the prohibition of the pass on theory are inapplicable. *See* Note, *Limiting a Regulated Pass On Exception to Illinois Brick*, 62 St. John's L. Rev. 647, 657 (1988); *see also Royal Printing Co. v. Kimberly-Clark Corp.*, 621 F.2d 323, 326 n.4 (9th Cir. 1980). In fact, all this "exception" recognized is the more general rule that only the injured can sue. "Cost-plus" was merely used as a label for an economic circumstance where a lower court could assume that an overcharge caused no injury to the direct purchaser because the lower court could be assured that no injury was left with the direct purchaser. The cost-plus "exception" thus was an example of a circumstance where the economic reasoning behind the direct purchaser rule does not apply and therefore indirect purchasers would not be precluded from maintaining an antitrust action. This case and *Allevato* present two other such circumstances.

3. Direct Purchasers, Such as Those in *Allevato* May Be Fully Insulated Against All Injuries.

The fourth scenario discussed above is an even more perfect pass on than that presented in this case; the indirect purchasers suffer all of the injury, while the direct purchasers suffer none. It is possible that the Respondent direct purchasers, which are profit-making utilities, suffered a decrease in profits due to end-users decreasing their demand for natural gas because of the increased price. Direct purchasers in some circumstances, however, do not suffer a loss of profits because they are prevented, by statute, by their charters or otherwise, from retaining a profit or excess revenue. This fact pattern is presented in *Allevato*, where the direct purchaser Counties are statutorily prohibited from collecting more than their costs.[7] The non-profit nature of the Counties is a substitute for the fixed quantity element discussed in *Illinois Brick*, which, in the words of the Court, "insulate[s] [the direct purchaser] from any decrease in its sales as a result of attempting to pass on the overcharge * * *." 431 U.S. at 736. The Counties are "insulated", that is, completely unaffected by any decrease in "sales", because they are statutorily prohibited from making a profit and their economic well being does not depend on the level of purchases of sewerage services.

The Seventh and Tenth Circuits are in harmony on the proposition that where no issue of injury due to decreased demand exists, a perfect pass on of overcharges justifies standing for indirect purchasers, not direct purchasers. Only the Sixth Circuit refuses to permit use of the pass on theory in such situations. *County of Oakland* v. *City of Detroit*, 866 F.2d 839, 849, 852 (6th Cir. 1989), *pets. for cert. pending sub nom., Allevato* v. *County of Oakland*, Nos. 89-56, 89-79, 89-101.

The issue of whether loss of profits by the direct purchaser due to a decrease in demand precludes use of the pass on theory was

[7]"[S]ituations occasionally arise which fail to fit with the Supreme Court's established exceptions, yet the overcharge seems to have passed through without any real threat of economic injury to the middleman. *See, e.g.*, *County of Oakland* v. *City of Detroit* 628 F. Supp. 610, 613 (E.D. Mich. 1986) * * *." Note, *Limiting a Regulated Pass On Exception to Illinois Brick*, 62 St. John's L. Rev. 647, 659 n.55 (1988).

the source of conflict between the Seventh Circuit and the Tenth Circuit. In *Panhandle*, Judge Posner reasoned that the element of damages caused by the decrease in demand is a completely different transaction, which may give rise to a suit by the direct purchasers, but should not preclude a suit by the indirect purchasers for the amount of the overcharge paid by them. 852 F.2d at 897. *Panhandle* observed that the true concern in *Illinois Brick* and *Hanover Shoe* arose when the direct and indirect purchasers were complaining about the *same* losses. 852 F.2d at 896-97. The Tenth Circuit below, *In re Wyoming Tight Sands Antitrust Cases*, 866 F.2d 891 (10th Cir. 1989), *cert. granted*, 58 U.S.L.W. 3349 (U.S. Jan. 16, 1990) (No. 88-2109), however, reasoned that the complexity of computing the loss of profits caused by a decrease in demand still justifies conferring standing only on the direct purchaser, even though the direct purchaser recovered, through a perfect pass on, 100 percent of the amount by which it was allegedly overcharged.

Therefore, even if this Court determines that the presence of injury due to a decrease in demand justifies granting standing to only direct purchasers, it should not foreclose the possibility of using the pass on theory in situations such as that in *Allevato*. The direct purchasers in *Allevato* not only passed on 100 percent of all overcharges, but were also insulated against any possible decrease in profits due to a decrease in demand because such decrease in demand was of no economic consequence to the direct purchasers.

B. Effective Enforcement of the Private Remedy Provisions of the Antitrust Laws Would Be Impaired By Granting Standing to Only Uninjured Direct Purchasers.

Elevating the uninjured direct purchaser to the preferred position of surrogate plaintiff here would completely destroy the remedial purposes of Section 4.[8] Treble damages were conceived not only to punish but, in the words of Senator Sherman, to counterbalance "the difficulty of maintaining a private suit against a com-

[8]*See also* Brief for the United States as *Amicus Curiae* in *Kansas* (Pet. for Cert.) at 10-11.

bination * * *." 21 Cong. Rec. 2456 (1890). The trebling of damages provision thus provided a safety net to ensure that persons whose injuries were comparatively small could still be made whole.[9] In the case of an uninjured direct purchaser, who need not be "made whole," the treble damages provision, while giving the direct purchaser some incentive to sue, does so at the expense of leaving the truly injured without any remedy. In *Hanover Shoe* and *Illinois Brick*, the incentive to sue and reward of treble damages at least went to a party that suffered some injury.

The goal of effective enforcement of the antitrust laws would be ill served by permitting *only* direct purchasers to sue in the presence of a perfect pass on. Specifically, a direct purchaser who perfectly passes on the effects of an overcharge would have no economic incentive to closely monitor the price of inputs and to sue if it detects an overcharge, because it does not have an economic interest in the price of goods or services subject to the unlawful overcharge.[10] Such a direct purchaser may, of course, have an incentive to sue brought about by the prospect of recovering trebled windfall damages — but this is not a proper incentive recognized in the antitrust laws. If, on the other hand, the direct purchaser was forced, pursuant to a statutory or regulatory requirement, to return any recovery, it would similarly lack any incentive to sue and become embroiled in complex litigation because it could not retain the fruits of victory. Whether the direct purchaser chose to sue or not to sue would be based on considerations other than making themselves "whole" — the underlying rationale of the remedial provisions of the antitrust laws. More likely than not, in the case of a regulatory perfect pass on, the direct purchasers, balancing the monetary and psychological costs of modern litigation against the result of being forced to pass on its recovery, would opt not to sue. Thus, the truly injured receive nothing because they are precluded from suing

[9]Other safety nets to assure that the antitrust laws will be enforced are *parens patriae* actions, *see* 15 U.S.C. § 15c (Supp. 1989), and class actions pursuant to Fed. R. Civ. P. 23, *see Hawaii*, 405 U.S. at 266.

[10]*See* Brief of the United States as *Amicus Curiae* in *Kansas* (Pet. for Cert.) at 11.

and the antitrust violator keeps all of its ill-gotten gain. This is clearly not the result envisioned by the drafters of the antitrust laws.

C. *Amici Curiae* Are Not Asking the Court to Carve Out Exceptions for Particular Markets.

Recognizing standing for indirect purchasers in this case and in *Allevato* would not "carve out" exceptions to the rule of *Illinois Brick* and *Hanover Shoe* for "particular markets," which the Court specifically rejected in *Illinois Brick*. 431 U.S. at 743-45. The Court in *Illinois Brick* was not cautioning against the pass on presented here and in *Allevato*, but was rather responding to an assertion by the indirect purchasers that the pass on theory should be permitted in certain markets where the economic conditions supposedly outweighed the policy considerations of *Illinois Brick* and *Hanover Shoe*.[11] In such situations, however, it was not clear that 100 percent of the burden of the overcharge fell on the indirect purchasers.

The Court can reverse in this case and in *Allevato* without inviting lower courts to engage in an exercise of line drawing or examining the economics of particular markets. Rather, the "line" presented here is quite clear and apparent from the nature of the relationship of persons along an economic chain of distribution, and thus would apply universally in all markets. No apportionment is necessary because we *know* that each and every penny of any overcharge *will* be paid by the end-users. *See Panhandle*, 852 F.2d at 898. When it is clear from the nature of a transaction (regardless of the market) that the direct purchaser cannot absorb any portion of an alleged unlawful overcharge, the direct purchaser cannot have standing to sue for the injuries sustained by paying such overcharge.[12]

[11]The indirect purchasers advocated creating exceptions for middlemen that resell goods without altering them, for contractors that add a fixed percentage mark-up to the cost of their materials in submitting bids or even for situations where "most" of the overcharge is passed on. *Illinois Brick*, 431 U.S. at 743-44.

[12]While the case at bar involves two state attorneys general suing in their capacity as *parens patriae*, the same issues are still at stake in *Allevato* because under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, 15 U.S.C. § 15c (1982), citizens of a state must have standing in order for the state

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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attorney general to sue in its *parens patriae* capacity. *See, e.g., Illinois Brick*, 431 U.S. at 730 n.14 ("this legislation did not alter the definition of which overcharged persons were injured within the meaning of § 4."); H. R. Rep. No. 499, 94th Cong., 1st Sess. 9 (1975) (the section creates no new substantive liability: each person on whose behalf the state attorney general is empowered to sue already has his or her own claim under Section 4, even if it is not exercised). The court below recognized that, *parens patriae* standing is, in reality, indirect purchaser standing, stating:

> This appeal involves a single issue: May *residential consumers who are indirect purchasers* of natural gas maintain a antitrust suit against the alleged antitrust violators?

Tight Sands, 866 F.2d at 1288 (emphasis added).

March 1, 1990

(12)

No. 88-2109

In The

Supreme Court of the United States

October Term, 1989

THE STATES OF KANSAS AND MISSOURI,
AS *PARENS PATRIAE*,

Petitioners,

v.

THE KANSAS POWER & LIGHT COMPANY
AND
UTILICORP UNITED, INC.,

Respondents.

BRIEF OF FORTY-SIX STATES AS AMICI CURIAE IN SUPPORT OF PETITIONERS

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IN THE
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Respondents.

BRIEF OF FORTY-SIX STATES AS AMICI CURIAE IN SUPPORT OF PETITIONERS

INTRODUCTION

The States of Alabama, Alaska, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Idaho, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigian, Minnesota, Mississippi, Montana, Nebraska, Nevada, New Hampshire, New

Jersey, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming, and Oklahoma ("Amici States") submit this brief in support of the Brief submitted by the Petitioners, the States of Kansas and Missouri.

INTERESTS OF THE AMICI STATES

The Attorneys General of the Amici States are the chief law enforcement officers of their states and are charged with the duty of enforcing both state and federal antitrust laws. In their parens patriae capacity, the Amici States, represented by their attorneys general, are authorized to bring federal antitrust actions to recover damages on behalf of the citizens of their states.1/ Using that authority, State attorneys general have represented consumers

1/ 15 U.S.C. § 15c. See also Georgia v. Pennsylvania R.R., 324 U.S. 439 (1945) (common law parens patriae authority).

efficiently and effectively. The Amici States have a vital interest in preventing the erosion of their parens patriae authority.

The States play a major role in antitrust enforcement and have a substantial interest in ensuring that the antitrust laws are interpreted in accord with sound antitrust policy and the prior decisions of this Court.

The Amici States support the contention of Kansas and Missouri that the instant suit on behalf of residential consumers is within the cost-plus exception to Hanover Shoe, Inc. v. United Shoe Machinery Corp., 392 U.S. 481 (1968) and Illinois Brick Co. v. Illinois, 431 U.S. 720 (1977). Kansas and Missouri assert that the cost-plus exception controls because the federal 2/

2/ See the Natural Gas Act, 15 U.S.C. § 717 et seq. (1982) and the Natural Gas Policy Act, 15 U.S.C. § 3301 et seq. (1982).

and state [3/] regulation of natural gas utilities creates a cost-plus pricing arrangement, passing on all of the increased cost of gas to the consumer.[4/]

The Tenth Circuit Court of Appeals rejected Kansas' and Missouri's contention, holding that the states could not bring a parens patriae action on behalf of their residential consumers who were indirect purchasers of the natural gas. See In re Wyoming Tight Sands Antitrust Cases, 866 F.2d 1286, 1294 (10th Cir. 1989), cert. granted sub nom. Kansas v. Kansas Power Light Co., 110 S. Ct. 833 (1990).

3/ See Kan. Stat. Ann. §§ 66-1,201, 66-1,206 (1985); Mo. Rev. Stat. §§368.250(5), 393.140(1), 393.270(2) (1986).

4/ Many of the Amici States have also enacted statutes that cause costs of natural gas production to be passed through to the ultimate consumers. See, e.g., Conn. Gen. Stat. § 16-196 (1989); Md. Code Ann. Art. 78 §54D (1980 Repl. Vol.); Mich. Comp. Laws § 460.6(h) (Cum. Supp. 1989); N.Y. Pub. Sev. L. §72-a (1989); Ohio Rev. Code §4905.302 (Supp. 1988); 66 Pa. Cons. Stat. Ann. §1307(f) (1984); Va. Code §56-235 (1986 Repl. Vol.).

SUMMARY OF ARGUMENT

Illinois Brick Co. v. Illinois, 431 U. S. 720 (1977), recognized that there are situations when indirect purchasers should be permitted to seek damages under Section 4 of the Clayton Act. This Court cited the "cost plus" exception and the "control exception" as examples of situations when the three concerns underlying the Illinois Brick decision - avoiding complicated apportionment of damages, ensuring vigorous enforcement of the antitrust laws, and avoiding duplicative damages - are met by allowing indirect purchasers to sue.

Regulatory cost-plus arrangements fall within the exception recognized by this Court. In the present case, rate regulation mandates a pass-through of fuel price increases. Yet, the Court below refused to allow residential consumers to sue for the overcharges because it erroneously believed that only cost-plus contracts for a "fixed quantity" came within the exception articulated in Illinois Brick. Illinois Brick

never stated, however, that a fixed quantity was essential to a cost-plus exception. Inherently, regulatory cost-plus contracts serve the economic function that fixed quantities serve in other cost-plus contracts.

The States, under the parens patriae authority granted by the Hart-Scott-Rodino Antitrust Improvements Act of 1976, are best able to represent residential consumers. Congress intended that the cost and burden of representing natural persons should shift to the States. Utilities will have much less incentive to sue because State public utility commissions may well force them to distribute their damage recoveries among residential consumers.

The present case cannot be distinguished from Illinois v. Panhandle Eastern Pipe Line Co., 852 F.2d 891 (7th Cir.) (en banc), cert. denied, 109 S.Ct. 543 (1988). In both cases, the regulatory schemes required utilities to pass price increases on to residential consumers. Yet, only the Seventh Circuit's decision in

Panhandle Eastern and not the Tenth Circuit's decision below, comports with both the policies of Illinois Brick and the parens patriae provisions of Hart-Scott-Rodino. The decision below should be reversed.

ARGUMENT

I.

THE TENTH CIRCUIT FAILED TO COMPREHEND THE PROPER APPLICATION AND POLICY CONCERNS OF ILLINOIS BRICK.

A.

THE RULE OF ILLINOIS BRICK RECOGNIZES EXCEPTIONS.

In Illinois Brick Co. v. Illinois, 431 U.S. 720 (1977), this Court construed section 4 of the Clayton Act, 15 U.S.C. § 15 (1982), and determined that, for purposes of recovering monetary damages under federal antitrust laws, direct purchasers were generally the appropriate plaintiffs. In most situations, therefore, an indirect purchaser is not injured within the meaning of Section 4 of the Clayton Act. See Illinois Brick, 431 U.S. at 733-37.

Illinois Brick extended the reasoning in Hanover Shoe, Inc. v. United Shoe Machinery Corp., 392 U.S. 481 (1968). There the Court held that a direct purchaser is injured by the full amount of any overcharge paid by it. A defendant cannot, in most cases, raise as a defense the fact that the direct purchaser had passed on the overcharge to indirect purchasers. See Hanover Shoe, 392 U.S. at 487-94.

The rule of Hanover Shoe does not bar the use of the passing-on defense in all situations. This Court stated:

> We recognize that there might be situations - for instance, when an overcharged buyer has a pre-existing "cost-plus" contract, thus making it easy to prove that he has not been damaged - where the considerations requiring that the passing-on defense not be permitted in this case would not be present.

Hanover Shoe, 392 U.S. at 494. Similarly, Illinois Brick recognized that courts should not bar the recovery of damages by indirect purchasers in all situations. The Court gave two distinct examples of exceptions to its own rule: the "cost-plus" exception and the "control

exception." 431 U.S. at 735-36. As this Court recently stated in California v. ARC America Corp., 109 S. Ct. 1661, 1666 n.6 (1989):

> In Illinois Brick, the Court was concerned . . . that at least some party have sufficient incentive to bring suit. Indeed, we implicitly recognized as much in noting that indirect purchasers might be allowed to bring suit in cases in which it would be easy to prove the extent to which the overcharge was passed on to them.

The Tenth Circuit, erroneously relying on Illinois Brick as precedent, denied Kansas and Missouri the right to maintain this parens patriae action because the regulatory cost-plus arrangement did not require the purchaser to buy a fixed quantity of natural gas. Yet, Illinois Brick involved neither a cost-plus contract, a fixed quantity contract, nor a regulatory cost-plus contract. Thus, as the Court of Appeals for the Seventh Circuit concluded in Illinois v. Panhandle Eastern Pipe Line Co., 852 F.2d 891 (7th Cir.) (en banc), cert. denied, 109 S. Ct. 543 (1988), a decision to deny the States the right to seek damages for their

residential consumers in regulatory cost-plus cases is "not dictated by precedent." 852 F.2d at 893.[5/]

In the absence of clear precedent, the Seventh Circuit's approach in Panhandle Eastern is appropriate. It analyzed the underlying purposes of Illinois Brick rather than pulling isolated words out of context. Indeed, the Supreme Court recognized that where facts differ markedly from Illinois Brick, a different result may be warranted. Illinois Brick, 431 U.S. at 735-36; see also ARC America, 109 S. Ct. at 1661 n.6.

5/ In Panhandle Eastern, the court confronted an issue identical to the issue before this Court: May a State Attorney General bring a parens patriae action for damages on behalf of residential consumers who purchased natural gas via a regulatory cost-plus arrangement? The court, after careful analysis, concluded that this case came within the "cost-plus" exception to Illinois Brick and that the action could be brought.

B.

THE CONCERNS OF ILLINOIS BRICK ARE RESOLVED IN COST-PLUS CONTRACTS.

The Illinois Brick Court identified three "federal purposes"[6/] that underlie its decision: (1) avoiding involving federal courts in unnecessarily complicated proceedings to apportion damages between direct and indirect purchasers, 431 U.S. at 737; (2) providing incentives to assure the presence of a private plaintiff able to discover the violation and ready and willing to pursue its rights vigorously--usually, but not always, a direct purchaser, 431 U.S. at 745; and (3) avoiding subjecting defendants to multiple and duplicative liability, 431 U.S. at 730-31. The Court determined that, on balance, denying the indirect purchaser the right to collect damages in that case best fulfilled these goals.

6/ See California v. ARC America Corp., 109 S. Ct. 1661 (1989).

As the Seventh Circuit recognized in Illinois v. Panhandle Eastern, in the case of a cost-plus contract, the concerns underlying Illinois Brick balance out differently, and the indirect purchaser may maintain a damages action. 852 F.2d at 894-95. The court stated, "There is no longer a problem of apportionment, because the whole of any price increase will have been passed on to the customers by virtue of the contract". Id. at 894. Similarly, there is no problem with subjecting defendants to multiple or duplicative recoveries. If the rule of Illinois Brick does not apply, the rule of Hanover Shoe would apply to prevent the direct purchaser from recovering damages for overcharges passed on to its customers, the residential consumers. Finally, although the direct purchaser might have information about the violation and an incentive to sue, these facts alone should not deprive indirect purchasers of the right to seek damages. See 852 F.2d at 895.

In the present case, the Tenth Circuit held that the cost-plus exception was not available primarily because the utilities' contracts with their customers do not require the consumer to purchase a "fixed quantity" of natural gas. 866 F.2d at 1292 (1989). Determined to read exceptions to Illinois Brick "narrowly," the Tenth Circuit noted that the cost-plus contract example discussed in Illinois Brick contained a fixed quantity. 866 F.2d at 1290 (1989).

As pointed out in Panhandle Eastern, however, Illinois Brick had no occasion or need to define a cost-plus exception with any precision. 852 F.2d at 893. Indeed, with its "narrow" reading of the dictum in Illinois Brick, the Tenth Circuit fell into the linguistic trap identified in Panhandle Eastern: "We do a disservice to the Court by wrenching its words out of context and giving them a talismanic significance; we make language a trap rather than a mode of communication." 852 F.2d. at 893. Contrary to the opinion of the Tenth Circuit, regulatory cost-plus

contracts fit within the cost-plus exception to Illinois Brick as neatly as cost-plus contracts for fixed quantities.

C.

REGULATORY COST-PLUS CONTRACTS CONSTITUTE EXCEPTIONS TO THE RULE OF ILLINOIS BRICK.

A regulatory scheme that provides for automatic pass-through of fuel price increases operates identically to a fixed quantity cost-plus contract. Regulation is a stand-in for the quantity requirement in an ordinary contract.

Regulatory cost-plus pricing imposes the burden of all price increases on the residential indirect purchasers. As Judge Posner explained in Panhandle Eastern, 852 F.2d at 896, a natural gas utility has a natural monopoly in supplying gas to consumers' homes. It could exert monopoly power in pricing in the absence of public utility rate regulation because residential consumers have no alternative, in the short term, to purchasing their gas requirements from the

utility. Id. In the short term, natural gas demand is inelastic. A residential consumer cannot convert to another energy source without an unreasonable investment in new heating, cooling or cooking equipment. If regulation keeps a utility's rates below its preferred level, the utility will almost always raise its rates to the highest level permitted. Id. Thus, a utility maximizes profit by increasing its rates to pass on the full amount of the overcharges it pays. Id.

Even if residential customers reduce consumption in response to higher rates, due to rate regulation, the utility's loss could not be passed along to residential consumers. Id. As the Seventh Circuit noted, although the utility itself sustains a loss, the loss arises from a different set of transactions (lost profits on potential sales not made) from the loss sustained by residential consumers (overcharges on sales made). Id. Thus, the apportionment problem of Illinois Brick does not arise. Id. at 896-97. Similarly, there will be no risk of multiple liability. Both the utility and the consumers

can seek damages because they will be suing for different injuries. Id. at 897. Any complexity in the present case involves determining the separate and distinct damages that residential consumers and utilities have suffered. In contrast, the Illinois Brick Court was concerned with the complexities added by allocating damages between direct and indirect purchasers. See 431 U.S. at 741-44.

Just as in the case of the fixed-quantity contract, a utility can force the entire cost increase onto its residential customers without sacrificing profits. First, rate regulation mandates pass through. Second, the essential nature of the product, coupled with the customers' lack of viable alternatives, makes this case in actuality a cost-plus contract for a fixed quantity. At the very least, consumers must fill their requirements at the increased rate, and the essential nature of the product limits the degree to which consumers can curtail purchases.

Finally, regulatory cost-plus contracts provide even greater reason than do ordinary cost-plus contracts to find Illinois Brick inapplicable. As the Panhandle Eastern court observed, if, as is likely, a public utility commission forces the utility to pass on to the consumers any damages that the utility recovers, "utilities will have no incentive to sue because they will have nothing to gain from suit." Id. at 895. Moreover, a utility may be reluctant to sue its supplier for fear of jeopardizing their relationship.

No doubt the respondent-utilities will protest, with vigor, that in the instant case the utilities actually did sue. Yet, if, as the Seventh Circuit suggests may happen, public utility commissions require these utilities and others to pass on their recoveries, utilities will become "most reluctant suitor[s]" with little stake in the outcome. Id. at 895. The Tenth Circuit's prohibition of damage actions by residential consumers would then leave no plaintiff "to discover and aggressively assert antitrust claims", In

re Wyoming Tight Sands Antitrust Cases, 866 F.2d at 1292, and the intent of Illinois Brick would be frustrated.

II.

THE STATES ARE THE BEST REPRESENTATIVES OF RESIDENTIAL CUSTOMERS IN REGULATORY COST-PLUS CASES.

The Seventh Circuit's decision in Panhandle Eastern recognizes the injustice that would result from dismissing this parens patriae lawsuit. Moreover, it reconciles Illinois Brick with the intent of Congress in enacting The Hart-Scott-Rodino Antitrust Improvements Act of 1976 (hereinafter "Hart-Scott-Rodino").[7/]

Title III of Hart-Scott-Rodino empowers State attorneys general to enforce the federal antitrust laws by representing their resident natural persons.[8/]

7/ Pub. L. No. 94-435, 90 Stat. 1383 (1976). Title III added Sections 4C through 4H to the Clayton Act, 15 U.S.C. §§ 15c through 15h.

8/ Hart-Scott-Rodino constitutes an express recognition by Congress that States are the best (Continued)

Throughout the thirteen years since its creation, the States' parens patriae authority has been a powerful and effective weapon against antitrust wrongdoing.[9/]

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representatives of their citizens. In enacting Hart-Scott-Rodino, Congress conferred this parens patriae authority in response to California v. Frito-Lay, Inc., 474 F.2d 774 (9th Cir.), cert. denied, 412 U.S. 908 (1973). In Frito-Lay, the Ninth Circuit had held that the state could not maintain an action as parens patriae on behalf of citizen-consumers to recover monetary damages for injuries suffered from an alleged price-fixing conspiracy among snack food manufacturers. 474 F.2d at 777. The court recognized that California had advanced what was "perhaps the most suitable" answer to deal with the problem of antitrust deterrence, but declined to usurp the power of the legislative branch. Id.

9/ See, e.g., In re Panasonic Consumer Electronics Antitrust Litigation, Civ. Action No. 89 Civ. 0368 SWK (S.D.N.Y. 1989)) ($16 million parens settlement available for 665,000 consumers obtained by 49 States and the District of Columbia); In re Minolta Camera Products Antitrust Litigation, 668 F. Supp. 456 (D. Md. 1987) ($4 million parens settlement available for over 300,000 consumers obtained by 36 states and the District of Columbia). See also Massachusetts v. First National Supermarkets, Inc., Civ. Action No. 85-3835 (D. Mass. 1990) (coupons and food donations worth over $8 million obtained for Massachusetts citizens); Connecticut v. Waldbaum, Inc., Dkt. No. H-87-263 (D. Conn. 1987); Connecticut v. Stop & Shop Co., Inc., Dkt. No. H-86-688 (D. Conn. 1988) (in settlement of related parens cases, coupons valued at $21 million obtained for Connecticut consumers); In re Mid-Atlantic Toyota Antitrust Litigation, 605 F. Supp. 440 (Continued)

Courts have recognized the superiority of the parens patriae action as a tool for representing the collective claims of a State's citizens.[10/] Indeed, "it is difficult to imagine a better representative of the retail consumer within a state than the state's attorney general." In re Ampicillin Antitrust Litigation, 44 F.R.D. 269, 274 (D.D.C. 1972); see also In re Antibiotic Antitrust Actions, 333 F. Supp. 278, 280 (S.D.N.Y. 1971).

The decision below deprives residential consumers of a remedy for the overcharges they paid. Because any given consumer will not suffer enough damage to justify expending substantial amounts of

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(D. Md. 1984) ($5 million parens settlement for over 35,000 consumers obtained by five States and the District of Columbia); Florida v. Cargo Gasoline Co., Civ. No. 82-875-J-B (M.D. Fla. 1986) ($1.2 million parens settlement obtained for Florida consumers).

10/ "The parens patriae action is plainly superior to the [Rule 23] class action as a mode for adjudication of collective claims." In re Montgomery County Real Estate Antitrust Litigation, 1988-2 Trade Cas. (CCH) ¶ 68,230 (D. Md. 1978). See also Pennsylvania v. Budget Fuel Co., 1988-2 Trade Cas. (CCH) ¶ 68,229 (E.D. Pa. 1988).

time and money in protracted litigation, this is precisely the situation the parens patriae provisions of Hart-Scott-Rodino were designed to remedy.

Nevertheless, the court below stated that permitting the States to bring these parens patriae cases would reduce the direct purchasers' incentive to sue and would shift "the cost and incentive of policing and enforcing the antitrust laws to the states." 866 F.2d at 1291. The court's perspective is totally at odds with the concerns of Congress. In enacting Hart-Scott-Rodino, Congress decided that in cases where natural persons like residential consumers are injured, the cost and burden of representing these citizens should shift to the States.

State attorneys general have the incentive and the experienced, specialized antitrust counsel to prosecute these suits vigorously on behalf of their citizens. In contrast, regulated utilities have little incentive to prosecute antitrust claims on behalf of

residential consumers.[11/] Unless State attorneys general are allowed to represent residential consumers in these cases, price fixers may elude justice. Thus, the need for State attorneys general to represent their citizens is particularly important in cases of regulatory pass-ons.

The Seventh Circuit's opinion is consistent with this Court's recent decision in California v. ARC America Corp., 109 S. Ct. 1661 (1989), which recognized that indirect purchasers could, in certain instances, be better antitrust enforcers than direct purchasers. See 109 S. Ct. at 1666, n. 6. A regulatory cost-plus contract is one of those instances.

III.

THIS CASE CANNOT BE DISTINGUISHED FROM PANHANDLE EASTERN IN ANY MEANINGFUL WAY.

In attempting to distinguish the instant case from Panhandle Eastern, the Tenth Circuit found that:

11/ See Section I(C), supra.

> The most important difference between Panhandle Eastern and this case may be that there was apparently no doubt in Panhandle Eastern that the entire overcharge was passed on. . . . In this case, the amount of the overcharge passed on may be an unresolved question of fact.

866 F.2d at 1293.[12/] Astonishingly, the court then undermined its "most important distinction" by stating, "However, even if we assume, as we do for the purpose of deciding the issue before us, that there was a perfect and provable pass-on of the allegedly illegal overcharge, we are not persuaded that the facts of this case would place this case into the narrow exception to the [Illinois Brick] rule." 866 F.2d at 1293 (emphasis added). The court, thus, concedes that this case, in its appellate posture, is indistinguishable from Panhandle Eastern.[13/]

12/ The question certified in this case states that "all or most" of the overcharges were passed on.

13/ The Tenth Circuit goes to great lengths to distinguish this case from Panhandle Eastern on additional bases as well. None of these distinctions is relevant to the holding of the case, however. See, e.g., note 15, infra.

Even if the Tenth Circuit did attach real meaning to the uncertainty implicit in the certified question about whether 100 percent of the overcharge had been passed on, this factor is not a valid distinction. The Panhandle Eastern court, confronted with the same question, stated:

> True, we can never be absolutely certain that regulation has resulted in a 100 percent pass through. . . . No counterfactuals are certain, but the doubts here are too small to warrant our insisting that this potentially serious antitrust violation, which may have caused consumers of natural gas to pay almost $50 million in higher prices, shall go unremedied, as it may if we accept Panhandle's view of the scope of Illinois Brick.

852 F.2d at 898.

In the present case, however, there is little doubt that the pass-on was complete. The district court found that the facts of the instant case and Panhandle Eastern are identical. In re Wyoming Tight Sands Antitrust Cases, 695 F. Supp. 1109, 1117 (D. Kan. 1988).14/ Kansas and Missouri also documented in

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14/ The Tenth Circuit incorrectly states that the
(Continued)

their Petition for Certiorari that their regulatory schemes require regulated utilities to pass price increases to their residential consumers, just as the Illinois regulatory scheme in Panhandle Eastern. See Petitioners' Petition for Certiorari at 4, n.3, In re Wyoming Tight Sands Antitrust Cases, 866 F.2d 1286, cert. granted sub nom. Kansas v. Kansas Power & Light Co., 110 S. Ct. 833 (1990); Panhandle Eastern, 852 F.2d at 895.15/ This Court must choose between

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Panhandle Eastern court found Tight Sands distinguishable from Panhandle Eastern. In fact, the Panhandle Eastern court identified the Tight Sands decision as one presenting a differing legal result which it would not follow.

15/ The Tenth Circuit states that utility companies here occupy "different levels on the distribution chain within two States" while Panhandle Eastern dealt only with the consumers of one utility. The court also notes that Kansas and Missouri have different regulatory schemes while the Panhandle Eastern court had to analyze only one scheme. These distinctions are immaterial. If any utility company is itself an indirect purchaser, then both the utility and its customers may be barred under the rule of Illinois Brick. However, if utilities are direct purchasers and pass on their damages to their indirect purchaser residential users via a cost-plus contract, then to that extent this case is precisely like Panhandle Eastern.

Panhandle Eastern and the Tenth Circuit's opinion in this case. The cases cannot be reconciled.

IV.

RECOGNIZING A REGULATORY COST-PLUS EXCEPTION IS CONSISTENT WITH ILLINOIS BRICK AND THE INTENT OF CONGRESS IN ENACTING HART-SCOTT-RODINO.

The Seventh Circuit's decision in Panhandle Eastern comports with both the policies of Illinois Brick and the parens patriae provisions of Hart-Scott-Rodino. The court recognized that permitting an action on behalf of residential purchasers of natural gas pursuant to regulatory cost-plus pricing does not offend the policies articulated in Illinois Brick. Further, the Seventh Circuit also permitted the Attorney General of Illinois to act in the manner authorized by Hart-Scott-Rodino. The parens patriae suit allowed the Attorney General to protect the residential consumers of his State and to ensure vigorous enforcement of the antitrust laws.

In contrast, the decision of the Tenth Circuit ignores the public policy concerns of Illinois Brick. Moreover, by expressing concern that Kansas and Missouri sought to "shift" to the States the responsibility of prosecuting antitrust cases on behalf of their citizens, the lower court subverts the important goals of Hart-Scott-Rodino. This decision hampers the ability of attorneys general to maintain suit when numerous citizens have been injured. Yet, Congress enacted Hart-Scott-Rodino to permit this type of suit. The Court should reaffirm the intent of Congress and permit the States to have the broadest possible power to vindicate the rights of injured citizens.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the United States Court of Appeals for the Tenth Circuit.

DATED: March 2, 1990

Respectfully submitted,

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Counsel of Record on Behalf
of Amici States

STATES OF KANSAS AND MISSOURI, ... Petitioners,

v.

UTILICORP UNITED INC., Respondent.

... to the United States ... for the Tenth Circuit

... CURIAE ... FEDERATION ... ENFORCEMENT

Jeffrey ...*
...
CURTIS, MALLET-PREVOST, COLT & MOSLE
... N.W.
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...

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QUESTION PRESENTED

In a private antitrust action under 15 U.S.C. § 15 involving claims of price fixing against the producers of natural gas, is a State a proper plaintiff as *parens patriae* for its citizens who paid inflated prices for natural gas, when the lawsuit already includes as plaintiffs those public utilities who paid the inflated prices upon direct purchase from the producers and who subsequently passed on most or all of the price increase to the citizens of the State?[1]

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[1] This is the question that the district court below certified for interlocutory appellate review at the request of the States who are the petitioners here. It is the question that was addressed by both the district court and the court of appeals below. *Wyoming Tight Sands Antitrust Cases*, 695 F.Supp. 1109, 1120 (D. Kan. 1988), *aff'd*, 866 F.2d 1286, 1289 (10th Cir. 1989) ("*Tight Sands*"). However, the States now ask this Court to address two variations on this question, each of which asserts that the utilities passed on *all* of the price increase. And they devote a significant part of their brief to arguing that the utilities in fact did pass on all of the price increase -- a factual question not resolved below.

It is inappropriate to ask this Court to resolve a question of fact. Also, as we discuss below, it is not likely that the utilities passed on *all* of the price increase, notwithstanding the States' regulatory schemes. We respectfully submit that the Court should therefore address the same question as the courts below.

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IN THE
SUPREME COURT OF THE UNITED STATES
October Term, 1989

No. 88-2109

THE STATES OF KANSAS AND MISSOURI,
AS PARENS PATRIAE,

Petitioners,

v.

UTILICORP UNITED INC.,

Respondent.

On Writ of Certiorari
to the United States Court of Appeals
for the Tenth Circuit

BRIEF OF AMICUS CURIAE
THE WASHINGTON LEGAL FOUNDATION
IN SUPPORT OF THE RESPONDENT

INTEREST OF THE AMICUS[2]

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[2] Counsel for all parties have consented to the filing of this *amicus* brief. Their written consents are on file with the Clerk of this Court.

The Washington Legal Foundation ("WLF") is a national nonprofit public interest law center with more than 120,000 members throughout the United States. WLF engages in litigation in matters promoting the free enterprise system, and the economic and civil liberties of individuals and businesses.

WLF believes that effective, rational enforcement of the antitrust laws supports the nation's free enterprise system. As this Court has observed:

> The Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade. It rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions.

Northern Pacific Railway v. United States, 356 U.S. 1, 4 (1958). WLF also recognizes, however, that if the antitrust laws are not applied effectively and rationally, they can become fetters upon competition, and deny consumers the benefits of "unrestrained interaction of competitive forces." Therefore, it is important both that the courts interpret the antitrust laws to prohibit only conduct that actually reduces consumer welfare, and that the courts deal efficiently with such conduct in order to deny those who conspire against the public interest any profit from their conduct and to deter others from following the same course. The question presented in the case at Bar concerns how best to ensure effective enforcement of the antitrust laws.

In this brief, we hope to bring to the attention of the Court relevant matter that has not already been brought to its attention by the parties. WLF brings a unique perspective to this case because it is committed to promoting and defending "free and unfettered competition as the rule of trade," and has no other interest in the resolution of this case, political or economic.

STATEMENT OF THE CASE

Utilicorp United Inc. ("Utilicorp") and The Kansas Power and Light Company ("KP&L") are public utilities operating in Kansas, Missouri, Nebraska and Oklahoma.[3] They purchase natural gas both for their own use in generating electricity, and for resale to their industrial, commercial and residential customers. They have brought suit under Section 4 of the Clayton Act, 15 U.S.C. § 15, alleging that certain natural gas producers in Wyoming and a pipeline company that transports gas from Wyoming to Utilicorp and KP&L conspired to raise the price of the natural gas in violation of the antitrust laws. The utilities claim as their damages both the extra cost of the natural gas they purchased, and the profits they would have earned on the additional natural gas they would have purchased and resold if the price had not been inflated as a result of the illegal conspiracy. The defendant natural gas producers and pipeline asserted as an affirmative defense that the utilities passed on any illegal overcharges to their customers, and therefore had not suffered any injury themselves.

The petitioners, the States of Kansas and Missouri, also have filed complaints against the same producers

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[3] When the writ of certiorari was granted, both of these companies were respondents. Subsequently, on March 22nd, the writ was dismissed as to KP&L pursuant to a stipulation among the parties. However, KP&L remains a plaintiff in this action.

and pipeline. The States seek to recover both the additional cost of gas purchased directly from the defendant pipeline by state agencies and municipalities, and, as *parens patriae* pursuant to Section 4C of the Clayton Act, 15 U.S.C. § 15c, the additional cost of natural gas purchased by residential gas customers in their states. Those customers purchased the gas directly from the utilities, and only indirectly from the defendant pipeline. The States do not seek to recover on behalf of any of the utilities' industrial or commercial customers, or on behalf of residential customers in Nebraska and Oklahoma. Purchases as to which the States seek to recover damages constitute less than 50% of the natural gas sold by the Utilicorp and KP&L.

The utilities moved to strike the defendants' "pass-on" affirmative defense, or in the alternative for partial summary judgment on that defense, and the district court granted partial summary judgment in favor of the utilities. The district court also recognized that the utilities' motions were "in reality, motions to dismiss the States of Kansas and Missouri in their *parens patriae* capacity," and *sua sponte* dismissed those aspects of the States' complaints. Thus, under the district court's decision, the utilities would be permitted to recover any illegal overcharge on all the gas they purchased from the pipeline, including all the gas they resold to customers, and the States would be permitted to recover any illegal overcharge on gas they or their subdivisions purchased directly from the pipeline. The utilities also would be entitled to recover the lost profits on any additional gas they would have sold absent the illegal overcharge.

The States sought and secured interlocutory appellate review of the district court's dismissal of their *parens patriae* claims. The court of appeals affirmed the district court's decision. On petition by the States,

this Court issued a writ of certiorari on January 16, 1990.

SUMMARY OF ARGUMENT

In *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977) ("*Illinois Brick*"), and *Hanover Shoe, Inc. v. United Shoe Machinery Corp.*, 392 U.S. 481 (1968) ("*Hanover Shoe*"), this Court established a general rule that only those who purchase directly from price-fixers or other antitrust law violators may recover damages under Section 4 of the Clayton Act, 15 U.S.C. § 15, for injury suffered as a result of the violation. This general rule bars indirect purchasers from securing compensation for any injury they suffer; instead, direct purchasers may secure compensation for both the injury they suffer and the injury indirect purchasers suffer.

From the outset, the Court recognized that this rule is not perfect. In a perfect world, every person injured as a result of an antitrust law violation would secure redress to the extent of its injury. But as the Court implicitly recognized, sometimes pursuing perfection can get in the way of achieving a good result. The Court observed that trying to determine the actual injury suffered by each person in a chain of purchasers "would require a convincing showing of . . . virtually unascertainable figures," and thus "[t]reble-damage actions would often require additional long and complicated proceedings involving massive evidence and complicated theories." *Hanover Shoe*, 392 U.S. at 493.

The Court also noted that each ultimate consumer would most likely have suffered little injury, and "would have only a tiny stake in a lawsuit and little interest in attempting a class action." *Id.* at 494. The Court was concerned that because of this, if antitrust injury had to be perfectly apportioned, no one might

bring suit against those who violated the antitrust laws, and the violators thus "would retain the fruits of their illegality." *Id.* As the Court explained in *Illinois Brick*, "[h]owever appealing [an] . . . attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness." 431 U.S. at 737.

General rules tend to have exceptions, and the Court has recognized a possible exception to the general rule against antitrust recovery by indirect purchasers. Specifically, the Court has indicated that a pass-on defense might be recognized, and a claim for damages by an indirect purchaser might be permitted, where the direct purchaser suffers *no* injury -- no uncompensated overcharge, and no lost profits -- because its customers are "committed to buying a fixed quantity regardless of price." *Illinois Brick*, 431 U.S. at 736.[4] The Court has stressed, however, the "narrow scope" of this exception, *id.* at 745, and has rejected "attempts to carve out exceptions . . . for particular types of markets." *Id.* at 744.

In the case at Bar, the States ask the Court to carve out an exception for a particular type of market, *i.e.*, for regulated markets where the regulatory scheme forces the direct purchaser to pass on most or all of any illegal overcharge. The States recognize that even if all of any illegal overcharge by the pipeline was passed on to the utilities' customers, the utilities have suffered some injury: lost profits on additional sales they would

[4] The Court has also said that "the pass-on defense might be permitted . . . where the direct purchaser is owned or controlled by its customer." *Illinois Brick*, 431 U.S. at 736 n.16. This exception is not relevant to the case at Bar because the utilities are neither owned nor controlled by their customers.

have made if the price of gas had been lower. The States also recognize that they cannot recover on behalf of the utilities' industrial or commercial customers, or on behalf of the residential customers in Nebraska and Oklahoma. Thus, even if the States' plea for a new exception were granted, the utilities would still have damage claims they could pursue. However, whether those claims would be large enough to induce the utilities to go through another 5-10 years of litigation is another question.

The States' proposed new exception should be rejected. Indeed, it seems to be included within two proposed exceptions that the Court has already rejected: for where "middlemen . . . resell goods without altering them," and for where "most of the overcharge is purportedly passed on." *Illinois Brick*, 431 U.S. at 743. What distinguishes these situations from the one exception that the Court has recognized -- where there is a cost-plus contract for a fixed quantity -- is that in the latter, the direct purchaser has suffered *no* injury whatsoever.

This is the correct place at which to draw the line on exceptions to the general rule against recovery by indirect purchasers. Where the direct purchaser has suffered injury for which no one else can recover damages, permitting indirect purchasers to recover some of their damages will substantially complicate the litigation and reduce the incentive for direct purchasers to pursue their claims, thus reducing the likelihood that the violators will ever be forced to disgorge all the fruits of their illegal behavior. Therefore, effective enforcement of the antitrust laws requires that the decision of the courts below be affirmed.

ARGUMENT

I. THIS CASE DOES NOT FIT WITHIN THE NARROW EXCEPTION TO THE DIRECT PURCHASER RULE ESTABLISHED BY *ILLINOIS BRICK.*

Since this case concerns who should be able to recover for antitrust injury, it is important to bear in mind that there are actually *three* types of injury that flow from price-fixing and other unreasonable agreements in restraint of trade. First, those who purchase the product pay more than they otherwise would -- what is referred to as the "overcharge." The direct purchaser may pass on some or all of this overcharge, in which case indirect purchasers are affected by it, too. Second, to the extent the direct purchaser resells the product -- with or without altering it -- the direct purchaser will resell less at the inflated price, and therefore lose the profit it would have earned on the additional sales it would have made at the non-inflated price. And finally, direct and indirect purchasers are injured to the extent they purchase other products to substitute, at a higher cost, for the product whose price is illegally inflated. For example, a utility that uses a mix of natural gas and coal to generate electricity will likely purchase more coal if the price of natural gas is artificially inflated. Similarly, consumers may purchase oil-fired furnaces instead of gas furnaces, or may purchase extra sweaters, or may just tolerate colder temperatures in their homes, if the price of natural gas is artificially inflated.

The lost profits of the direct purchasers and the substitution costs of the indirect purchasers are directly related: if the price of the product were not inflated, the indirect purchasers would spend their money on the product instead of the substitutes, and the direct purchaser would earn its profits on those sales. Therefore, it would be duplicative to permit recovery of both the direct purchaser's lost profits and the indirect purchasers' substitution costs. And as difficult as it may be to determine lost profits, it is still far easier than attempting to determine substitution costs.

Ideally, whenever prices are artificially inflated as a result of an antitrust law violation, each person who suffers any injury would recover its damages. As a practical matter, however, calculating these damages would be extremely difficult, if not impossible -- and even just making the effort would necessitate extremely long and complex proceedings. This tension between perfection and reality is the focus of *Hanover Shoe* and *Illinois Brick*.

In *Hanover Shoe*, the plaintiff shoe manufacturer alleged that it had been injured by the defendant machinery manufacturer's refusal to sell, and insistence upon leasing, its machinery -- behavior that had earlier been found to be an antitrust violation. The defendant argued, however, that the plaintiff had not really been injured because any extra cost it had incurred was passed on to its customers in the form of higher prices.

This Court did not reject this argument as a theoretical proposition. It was concerned instead with the practical implications of permitting such a defense. First, the Court was concerned that this would greatly complicate already complicated treble-damage actions. The Court observed that "[a] wide range of factors influence a company's pricing policies," that it is also "difficult to determine, in the real economic world rather than an economist's hypothetical model, . . . what effect a change in a company's price will have on its total sales," that "costs per unit for a different volume of total sales are hard to estimate," and that even if all

this were done, "there would remain the nearly insuperable difficulty of demonstrating that the particular plaintiff could not or would not have raised his prices absent the overcharge or maintained the higher price had the overcharge been discontinued." 392 U.S. at 492-93. The Court therefore concluded that permitting the passing-on defense "would often require additional long and complicated proceedings involving massive evidence and complicated theories." *Id.* at 493.

The Court's second concern was that permitting the passing-on defense would reduce the likelihood that anyone would actually bring suit, and therefore increase the likelihood that those who violate the antitrust laws "would retain the fruits of their illlegality." *Id.* at 494. The Court observed correctly that if the passing-on defense were permitted all the way down the chain of purchasers, the people entitled to assert claims would be ultimate consumers, who "would have only a tiny stake in a lawsuit and little interest in attempting a class action." *Id.*

Therefore, the Court concluded that as a general rule, an antitrust law violator would not be permitted to assert a passing-on defense.

These considerations were revisited in *Illinois Brick*, with the same result. In that case, the State of Illinois brought suit on behalf of itself and 700 local governmental entities, alleging that the defendant manufacturers of concrete blocks had fixed prices on those blocks in violation of the antitrust laws. These bricks were purchased from the defendants by masonry contractors and used by them to build masonry structures; those structures then were incorporated into entire buildings by general contractors, who sold the complete projects to the plaintiffs. Thus, the plaintiffs were

indirect purchasers of the blocks, three levels down from the unlawful conspiracy.

The Court held again that as a general rule, "the overcharged direct purchaser should be deemed for purposes of § 4 to have suffered the full injury from the overcharge." 431 U.S. at 726, 746. It reiterated its concern about the practical effect of trying to trace effects beyond direct purchasers, observing that "[h]owever appealing [an] . . . attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness." *Id.* at 737. The Court was greatly concerned about reducing the incentive for direct purchasers to bring treble-damage actions, fearing that this "could seriously impair this important weapon of antitrust enforcement." *Id.* at 745.

Even as the Court established the general rule that only direct purchasers would have standing to sue under Section 4 of the Clayton Act, it acknowledged that there could be exceptions:

> We recognize that there might be situations -- for instance, when an overcharged buyer has a pre-existing 'cost-plus' contract, thus making it easy to prove that he has not been damaged -- where the considerations requiring that the passing-on defense not be permitted . . . would not be present.

Hanover Shoe, 392 U.S. at 494. In fact, however, an overcharged buyer with a "cost-plus" contract will be damaged -- in terms of lost profits -- unless its customer is obligated to buy as much of the product at the inflated price as at a lower price. Perhaps for this reason, the Court clarified this exception in *Illinois Brick*, limiting it to situations where "the [direct]

purchaser is insulated from any decrease in its sales as a result of attempting to pass on the overcharge, because its customer is committed to buying a fixed quantity regardless of price." 431 U.S. at 736. Plainly, this exception does not apply to the situation at Bar: none of the utilities' residential customers are committed to buying a fixed quantity of natural gas regardless of price.

The Court in *Illinois Brick* stressed "the narrow scope it intended for any exception" to the general rule. *Id.* at 735-36. It acknowledged that the difficulties and uncertainties that had been the focus of its concern in *Hanover Shoe* "will be less substantial in some contexts than in others," but the Court rejected the idea of "carv[ing] out exceptions to the *Hanover Shoe* rule for particular types of markets." *Id.* at 743-44. As the Court explained:

> the process of classifying various market situations according to the amount of pass-on likely to be involved and its susceptibility of proof in a judicial forum would entail the very problems that the *Hanover Shoe* rule was meant to avoid. The litigation over where the line should be drawn in a particular class of cases would inject the same "massive evidence and complicated theories" into treble-damages proceedings, albeit at a somewhat higher level of generality. . . . *Hanover Shoe* itself implicitly discouraged the creation of exceptions to its rule barring pass-on defenses, and we adhere to the narrow scope of exemption indicated by our decision there.

Id. at 744-45.

II. THE COURT SHOULD DECLINE TO CARVE OUT A NEW EXCEPTION TO THE HANOVER SHOE/ILLINOIS BRICK RULE.

Notwithstanding this discouragement, the States in the case at Bar are asking the Court to carve out an exception to the *Hanover Shoe/Illinois Brick* rule for a particular type of market. We respectfully submit that the Court should again decline to do so.

The States first argue that as a result of their regulatory schemes, the entire overcharge to the utilities on the gas they sold to residential customers was passed on to those customers, and is easy to compute. This is, however, an unresolved question of fact: the district court made no findings of fact concerning how much of the natural gas overcharges were passed on to the utilities' industrial, commercial or residential consumers. Moreover, it is intuitively implausible that *all* of any overcharge was passed on even to the residential consumers. For example, there may be a time lag between when the price changes on gas purchased by the utilities and when they adjust the rate their residential customers pay for gas. Some consumers may move or for other reasons terminate their service during that time period. What happens to the overcharge attributable to the gas they used? Perhaps only a relatively small proportion of any overcharge is not passed on, but calculating it would likely entail the "massive evidence and complicated theories" that this Court has said should not be introduced into treble-damage actions. *Hanover Shoe*, 392 U.S. at 493; *Illinois Brick*, 431 U.S. at 745.

Furthermore, even if the entire overcharge on the gas used by residential customers was passed on to them and could be calculated easily, denying the utilities the right to recover this element of the antitrust injury would reduce their incentive to sue. The States

agree that only the utilities may seek damages as to some of the antitrust injury -- such as the overcharges borne by the utilities themselves and by their industrial and commercial customers, and the utilities' lost profits, which reflect their customers' substitution costs. Any reduction in the utilities' incentive to sue increases the likelihood that they will not sue -- and that therefore the price-fixers will retain some of the fruits of their unlawful activity. Avoiding this is the second major goal of the *Hanover Shoe/Illinois Brick* general rule.

Even assuming a perfect pass-on of any overcharges, there would still be a critical difference between the situation here and the exception suggested in *Hanover Shoe* and *Illinois Brick*: here, no customer is committed to buying a fixed quantity regardless of price. The States argue (Brief at 22) that this Court "cannot have intended to prescribe a mechanical 'fixed-quantity' test for determining whether to allow indirect purchaser suits," citing *Illinois v. Panhandle Eastern Pipe Line Company*, 852 F.2d 891 (7th Cir.), *cert. denied*, 109 S. Ct. 543 (1988) ("*Panhandle Eastern*"). The States assert (Brief at 22) that "[t]he importance of a fixed-quantity contract is to ensure that the direct purchaser has passed on the entire overcharge rather than absorbing some of it to avoid losing customers."

We disagree. The cost-plus aspect of a cost-plus/fixed-quantity contract tends to ensure that the entire overcharge has been passed on to the indirect purchaser. The purpose of the fixed-quantity requirement is to ensure that the entire injury has been borne by the indirect purchaser.

If there is a perfect pass-on of the overcharge without a fixed-quantity requirement, one part of the antitrust injury -- the lost profits -- will be suffered by the direct purchaser, and another part -- the overcharge

-- will be suffered by the indirect purchaser. As a result, neither might have the incentive to sue. To avoid this, the Court authorized the direct purchaser to sue for the overcharge, too. By contrast, with a fixed-quantity requirement, the full burden of the antitrust law violation falls upon the indirect purchaser because the direct purchaser does not suffer any lost profits, and therefore the indirect purchaser has as much incentive to sue as anyone could have.[5]

The States also argue that the utilities might not have sufficient incentive to sue because the state regulatory authorities might order the utilities to pass on any recovered overcharges to their customers. But as the court of appeals observed, "a utility filed first in this case. . . . It is reasonablee to assume that the public utilities must believe there is something for their benefit in pursuing these actions." *Tight Sands*, 866 F.2d at 1291-92. Moreover, the States can ensure that utilities have incentive to sue whenever they suffer antitrust injury by refusing to include in a utility's rate base any costs incurred as a result of an antitrust law violation for which the utility does not seek redress.

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[5] In *Panhandle Eastern*, the Seventh Circuit misapprehended the significance of the fixed-quantity requirement. That court's confusion is further evidenced by its statement that a requirements contract is the equivalent of an agreement to take a fixed quantity. 852 F.2d at 898. Judge Posner wrote for the court that "a buyer under a requirements contract does not have discretion as to the amount to take under the contract," *id.*, but this simply is not correct. The buyer under a requirements contract has total discretion as to the amount to take under the contract: it is bound only not to buy any of the product from any other source. If the price of the product goes up, the buyer may -- and most likely will -- purchase less of it. Indeed, the residential customers of the utilities here had, in effect, requirements contracts with the utilities for their natural gas: as a practical matter, they had to purchase all their natural gas from the utilities, but they could (and did) reduce their purchases as the price of natural gas increased.

The States contend (Brief at 17) that "state attorneys general, as representatives of the consumers actually sustaining damages, are the most reliable parties to pursue the overcharges," and point to the fact that only two of the fifty regulated gas utilities in the relevant service areas in Kansas and Missouri have brought suit. On the other hand, the attorneys general of only two of the four states in which Utilicorp and KP&L distribute natural gas have brought suit. Thus, only Utilicorp and KP&L are seeking damages on account of the overcharge applicable to natural gas consumed by residential customers in Nebraska and Oklahoma.[6]

Finally, the States argue (Brief at 23) that Section 4C of the Clayton Act gives them "standing to bring antitrust suits on behalf of 'natural persons' injured by antitrust violations, regardless of whether those persons are direct or indirect purchasers." Indeed, the States seem to be arguing that there should be a preference for *parens patriae* actions. They are wrong on both counts.

> First, this Court has already held that Section 4C did not alter the definition of which overcharged persons were injured within the meaning of § 4. It simply created a new procedural device -- *parens patriae* actions by States on behalf of their citizens -- to enforce existing rights of recovery under § 4. . . . [T]he *parens patriae* provision "creates no new substantive liability"; . . . it was intended only as "an alternative means . . . for the vindication of existing substantive claims."

[6] The forty-six states who have joined as *amici curiae* in support of the petitioners assert (Brief at 21) that "[s]tate attorneys general have the incentive and the experienced, specialized antitrust counsel to prosecute these suits on behalf of their citizens." Perhaps some of those forty-six attorneys general have "experienced, specialized antitrust counsel" on their staffs, but Kansas and Missouri here, and Illinois in *Panhandle Eastern*, are all represented by private law firms, who are presumably motivated by the same incentive as the private law firms representing the utilities.

Illinois Brick, 431 U.S. at 733 n.14, quoting H.R.Rep. No. 94-499 at 9 (1975), 1976 U.S. Code Cong. & Admin. News 2572, 2578. Thus, the *parens patriae* claims of the States here are only as good as would be claims brought by residential customers on their own behalf.

Second, there is no reason to favor *parens patriae* actions over actions brought by private parties. Indeed, if anything, they should be disfavored because they bring with them a risk that political considerations will affect the litigation process. A state attorney general might bring a case that really should not be brought in order to secure publicity, or might refrain from bringing a case that should be brought in order to avoid offending a supporter. Similarly, political considerations could affect a state attorney general's willingness to settle a case. *Parens patriae* actions have a role to play where there is no private plaintiff ready, willing and able to seek relief for antitrust injury suffered by consumers who are direct purchasers. There is no reason, however, to create a special rule to encourage them on behalf of consumers who are indirect purchasers.

The essence of the States' argument is really that the *Hanover Shoe/Illinois Brick* rule is not perfect. This is true -- and the Court has acknowledged as much from the outset. The States complain bitterly (Brief at 19) because the decision below denies "truly-injured parties of their claims." This, too, is true, and also has

been recognized by this Court as a likely effect of the rule against antitrust recovery by indirect purchasers:

> It is true that, in elevating direct purchasers to a preferred position as private attorneys general, the *Hanover Shoe* rule denies recovery to those indirect purchasers who may have been actually injured by antitrust violations.

Illinois Brick, 431 U.S. at 746. But to paraphrase Winston Churchill's observation about democracy, no one pretends that the *Hanover Shoe/Illinois Brick* rule is perfect or all-wise. Indeed, it may be the worst way to avoid over-complicating treble-damage actions and to ensure that someone will have the incentive to sue for redress of antitrust injury -- except for all those other approaches to this problem that have been suggested from time to time. Almost from the day *Illinois Brick* was decided, Congress has been trying to find some way to permit indirect purchasers to seek redress for antitrust injury. *See, e.g.*, S. 1962, 100th Cong., 1st Sess. (1987); S. 2022, 99th Cong., 2d Sess. (1986); S. 2481, 99th Cong. 2d Sess. (1986); S. 915, 98th Cong., 1st Sess. (1983); S. 300, 96th Cong., 1st Sess. (1977); S. 1874, 95th Cong., 1st Sess. (1977); H.R. 2060, 96th Cong., 1st Sess. (1979); H.R. 2204, 96th Cong., 1st Sess. (1979); H.R. 8359, 95th Cong., 1st Sess. (1977). But nothing has come of any of these efforts because Congress has never been persuaded that any particular proposed change would yield on balance a better result than this Court's rule. For the same reason, the Court should now decline the petitioners' request that it modify the *Hanover Shoe/Illinois Brick* rule.

CONCLUSION

The judgment of the Tenth Circuit should be affirmed.

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